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STATE TAXATION — AN OVERVIEW

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I. Introduction

This Legislative Guide is entitled *State Taxation: An Overview* and is intended to serve as a general introduction to the subject.

The Guide is one of many Legislative Guides published by the Legal Division of the Legislative Services Agency.¹ If more information on a particular tax-related topic is desired, the following Guides may also be consulted:

- Charitable Property Tax Exemption
- Education Finance
- Gambling — Casinos and Racetracks
- Local Property Tax
- Road Use Tax Fund
- State Taxation — Corporate Income Tax and Franchise Tax
- State Taxation — Individual Income Tax
- State Taxation — Sales and Use Taxes
- Unemployment Compensation Benefits in Iowa
- Urban Renewal and Tax Increment Financing

A. Purpose and Scope

The purpose of this Guide is to familiarize the reader with the general landscape of taxation in Iowa, including a brief summary of the limitations on state taxation in the United States, a brief description of the taxes imposed by the state of Iowa, and an overview of the revenues generated by those taxes.

The Guide does not evaluate the fairness of Iowa taxes, recommend changes to Iowa tax law, or compare taxation in Iowa to taxation in other states. Nor does the Guide discuss the history of taxation in Iowa; it focuses instead on the current state of the law.

Finally, while the Guide is intended to inform as to the general legal issues involved with state taxation in Iowa, the reader is cautioned against relying on it as a source of legal advice or using it to prepare or file Iowa tax returns.

B. A Note About References

A number of abbreviations and shorthand references are used in this Guide:

1. Unless otherwise indicated, “Iowa Code” refers to the 2016 Iowa Code.
2. “Internal Revenue Code” and “IRC” refer to the federal Internal Revenue Code of 1986 as in effect on January 1, 2015.
3. “Iowa Administrative Code” refers to the Iowa Administrative Code current through October 2015.

¹ <https://www.legis.iowa.gov/publications/legalPubs/legisGuides>.



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4. “CY” means calendar year.
5. “FY” means fiscal year and refers to the state fiscal year ending on June 30 of the year designated. For example, “FY 2016” refers to the state fiscal year beginning July 1, 2015, and ending June 30, 2016.

II. Federal Constitutional Limitations on State Taxation

State law is not the only body of law that affects tax policy in Iowa. The United States Constitution contains a number of provisions that circumscribe Iowa’s power to levy taxes in a federal system. Some of these provisions serve to protect the interests of the federal government and some serve to protect the interests of individual taxpayers. All of them are appropriately included in any overview of state taxation because they represent the limits of permissible action available to states in the formation and implementation of tax policy. It is helpful to understand the federal constitutional framework for state taxation because this framework has frequently impacted the design and administration of state tax laws.

A. The Commerce Clause

1. In General

Economic activity in Iowa reaches beyond the borders of the state, and the tax policies implemented in Iowa can have consequences beyond those borders as well. For this reason, the most significant of all federal constitutional limitations on state taxation is the Commerce Clause.

The Commerce Clause gives Congress an express grant of power to “regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes.”² The U.S. Supreme Court has consistently interpreted this power to also contain a negative command, referred to as the “negative” or “dormant” Commerce Clause, that prohibits states from discriminating against, or unduly burdening, interstate commerce in the absence of Congressional approval.

At one time in the U.S. Supreme Court’s history, the Commerce Clause was interpreted as creating a zone of commerce entirely immune from taxation by the states. This formalism has evolved into a more flexible, substantive approach to state taxes and a recognition by the Court that it was not the intent of the founders to “immunize such commerce from carrying its fair share of the costs of the state government in return for the benefits it derives from within the State.”³ Thus today, states may tax interstate commerce if certain requirements are satisfied. The Court has developed a four-part test to determine the validity of state tax laws under the Commerce Clause: the tax must be applied to an activity with a substantial nexus in the state, must be fairly apportioned, must not discriminate against interstate commerce, and must be fairly related to the services provided by the state.⁴

² U.S. Const. art. I, §8, cl. 3.

³ *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450, 461-462 (1959).

⁴ This four-part test, while having antecedents in case law, was definitively adopted as the Court’s primary analytical framework in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977). Subsequent cases have further refined the meaning and application of the test, but this case and the four-part test it endorsed remain the key precedent for evaluating the validity of state taxes under the Commerce Clause.



a. Substantial Nexus. Substantial nexus, or “nexus”, under the Commerce Clause refers to the level of connection that a taxpayer must have with a state before being subject to taxation. It is the first step in determining whether a state has the power to exercise its taxing authority over a particular taxpayer. Although the Due Process Clause also requires a similar connection, the Commerce Clause requirement is more extensive because it concerns the effects of state regulation on the national economy.⁵

What constitutes nexus is not necessarily the same for every type of tax. The Court held in *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992), that “physical presence” in the state is required to create nexus for purposes of sales and use taxes.⁶ In *Quill*, a mail-order seller with no property or employees in North Dakota solicited sales from North Dakota residents via mail and telephone. North Dakota attempted to require Quill to collect use tax from customers on sales made outside the state. The Supreme Court held it was a violation of the Commerce Clause to require an out-of-state mail-order seller to collect a state’s sales or use tax if the seller did not have a “physical presence” within the state.⁷ Although the requisite type and amount of physical presence needed to create constitutional sales and use tax nexus has been the subject of debate,⁸ *Quill* nonetheless affirmed a bright-line rule that to date has not been reexamined by the Court or addressed legislatively by Congress.⁹

The Court has not explicitly extended this physical presence rule to other types of tax, but has instead emphasized a “flexible approach based on economic reality and the nature of the activity giving rise to the income that the state seeks to tax.”¹⁰ Several state courts, including Iowa, have used these facts to pursue a more flexible “economic presence” standard for income tax nexus.¹¹ The Iowa Supreme Court has

⁵ *Quill Corp. v. North Dakota*, 504 U.S. 298, 312-313 (1992).

⁶ See also *National Bellas Hess, Inc. v. Department of Revenue of Ill.*, 386 U.S. 753 (1967), which was affirmed in part by the *Quill* ruling.

⁷ *Quill*, 504 U.S. at 314-319.

⁸ The Court has rejected the argument that the slightest physical presence in a state is enough to create constitutional nexus. *National Geographic Society v. California Board of Equalization*, 430 U.S. 551, 556 (1977). But it has held that nexus was created by a mail-order vendor with two offices and employees in the state, even though the offices had nothing to do with the mail-order operations. *Id.* In *Quill*, the Court held that mail and telephone solicitation of customers in the state, and the holding of title to “a few floppy diskettes” in the state, was insufficient to amount to physical presence. See *Quill*, 504 U.S. at footnote 8. See also *National Bellas Hess*, 386 U.S. 753 (1967) (receipt of mail provides insufficient nexus). See also *Standard Pressed Steel Co. v. Wash. Department of Revenue*, 419 U.S. 560 563-564 (1975) (although dealing with gross receipts taxes, holding in-state presence of one full-time employee sufficient to support constitutional nexus on out-of-state entity).

⁹ Because Congress has the power to regulate interstate commerce, it has the power to modify the holding of *Quill* through legislation.

¹⁰ *KFC Corporation v. Iowa Department of Revenue*, 792 N.W.2d 308, 314 (Iowa 2010) (recounting by Iowa Supreme Court of previous U.S. Supreme Court cases involving challenges to state income taxes).

¹¹ *Id.* In *KFC*, KFC Corp. was a Delaware Corporation with a principal place of business in Kentucky. KFC Corp. licensed its trademarks and other intellectual property to KFC restaurants in Iowa that are independently owned franchisees. KFC Corp. owned no property in Iowa and had no employees in Iowa. The Court regarded this as sufficient connection to Iowa to amount to the functional equivalent of “physical presence” under the Commerce Clause because the franchisees were firmly anchored in Iowa and the transactions produced revenue from use in Iowa. Interestingly, the Court also held physical presence is not required under the Commerce Clause in order for Iowa to impose an income tax on revenue earned by an out-of-state corporation arising from the use of intellectual property by franchisees located within Iowa. See also the Matter of: *Jack Daniels Properties, Inc. and Southern Comfort*



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ruled that physical presence is not required under the dormant Commerce Clause in order to impose the income tax on revenue earned by an out-of-state corporation that licenses intangibles used in Iowa because the corporation receives the “benefit of an orderly society within the state” for the production of income.¹²

b. Fair Apportionment. The “central purpose behind the apportionment requirement is to ensure that each State taxes only its fair share of an interstate transaction.”¹³ Fair apportionment is concerned with the avoidance of state tax formulas that create multiple taxation and gross distortions of income. The Court imposes no single method or formula for apportioning a tax, but instead looks to whether the law is internally and externally consistent.¹⁴

The “internal consistency test” looks to the structure of the tax scheme to determine whether its “identical application by every State in the Union would place interstate commerce at a disadvantage as compared with commerce intrastate.”¹⁵ The “external consistency test” asks “whether the State has taxed only that portion of the revenues from the interstate activity which reasonably reflects the in-state component of the activity being taxed.”¹⁶

The apportionment of sales taxes is generally not required because the sale of goods and services is viewed as discrete events occurring at the place of sale.¹⁷ The

Properties, Inc. v. Iowa Department of Revenue, Dkt. No. 09 DORFC 002; 004 (Iowa Dep’t of Inspections and Appeals, July 28, 2011) (released March 7, 2012) (holding that it was not a violation of the Commerce Clause to impose the corporate income tax on subsidiary owners of the “Jack Daniels” and “Southern Comfort” trademarks whose only connection to Iowa was through the licensing of the trademarks to a parent corporation who marketed and sold whiskey bearing trademarks in Iowa). See also *Geoffrey, Inc. v. S.C. Tax Comm’n*, 313 S.C. 15 (1993) (South Carolina Supreme Court holding physical presence not required to impose state income tax on out-of-state franchisors who earned income based on franchise activities within state). See also *Capital One Bank v. Comm’r of Revenue*, 453 Mass. 1 (2009) (Massachusetts Supreme Court adopting flexible economic substance analysis rather than physical presence test in context of franchise and income taxes). See also *Tax Comm’r v. MBNA Am. Bank, N.A.*, 220 W.Va. 163 (2006) (Supreme Court of Appeals of West Virginia adopting an economic presence analysis in context of franchise and income taxes).

¹² *KFC*, 792 N.W.2d at 328.

¹³ *Goldberg v. Sweet*, 488 U.S. 252, 260-261 (1989).

¹⁴ *Container Corp. of America v. Franchise Tax Board*, 463 U.S. 159, 169 (1983).

¹⁵ *Comptroller of the Treasury of Maryland v. Wynne*, 135 S.Ct. 1787, 1802 (2015). The test helps the Court differentiate between tax laws that are inherently discriminatory against interstate commerce (typically unconstitutional), and tax laws that could create double taxation of income, or disparate incentives to engage in interstate commerce, only because of the interaction between two different but nondiscriminatory tax laws (typically constitutional).

¹⁶ *Goldberg*, 488 U.S. at 262.

¹⁷ *Oklahoma Tax Commission v. Jefferson Lines, Inc.*, 514 U.S. 175 (1995). In *Jefferson*, a common carrier collected sales tax in Oklahoma on bus tickets sold for travel within Oklahoma, but not for interstate travel, even though such travel originated in Oklahoma. The Court determined that Oklahoma could require Jefferson to collect sales tax on the full value of the bus tickets for interstate travel, without apportionment to other states. The tax was internally consistent because if every state had the same tax, tickets would only be taxed once in the originating state. The tax is externally consistent because no other state besides Oklahoma could claim to be the site of the sale, i.e., the place where the agreement, payment, and delivery of the bus service originated. Thus, the purchaser of the bus ticket is not subjected to multiple taxation in other states. This can in some cases also be true for other consumption or excise taxes that bear similarities to a sales tax. For example, in *Goldberg*, the Court upheld an Illinois excise tax on interstate telephone calls that originated or terminated in Illinois, and that were charged to an Illinois service address, regardless of where the call is billed or paid, because it had many of the characteristics of a sales tax, i.e., it was assessed on the individual consumer, collected by the retailer, and accompanied the retail purchase of an interstate telephone call. Moreover, apportioning would have created “insurmountable administrative and technological barriers.” *Goldberg*, 488 U.S. at 264-265.



apportionment of taxes on or measured by income or gross receipts is generally required.¹⁸ This can be a complex task, especially when dealing with businesses that operate in several states, that are composed of several different business units, or that are organized as several separate entities. As a result of this complexity, the Court developed the “unitary business principle” to permit States to tax businesses on an apportionable share of their multistate business.¹⁹ This principle rests on two grounds: one, a state need not isolate a unitary business’s in-state activities from the rest of the business, but may tax an apportioned share of the entire unitary business; and two, the state may not tax an out-of-state corporation’s income that is derived from an “unrelated business activity” which constitutes a “discrete business enterprise.”²⁰ For Iowa tax purposes, a unitary business is one carried on partly inside Iowa and partly outside Iowa, where the portion carried on in Iowa depends on or contributes to the business outside Iowa.²¹ In determining whether a unitary business exists, the overriding consideration is whether there has been an exchange or transfer of value, which may be evidenced by “functional integration, centralization of management, and economies of scale.”²²

Many states determine their apportionable share of a unitary business’s income by using a three-factor formula that takes into account the average of a specified percentage of the business’s total sales, property, and payroll made or located in the state. Iowa uses a single-factor sales formula based on the amount of gross sales made within Iowa or gross receipts earned within Iowa.²³

¹⁸ This was most recently addressed in *Wynne*, where the Court held that the Commerce Clause applies to resident individuals who are subject to personal income taxes in their state of residence. In *Wynne*, Maryland counties imposed an income tax on all the income of Maryland residents, but did not provide a tax credit for income taxes paid to other states on income earned in those states. The Court held the Maryland tax scheme failed the “internal consistency test,” and thus violated the Commerce Clause, because it caused individuals to pay more total income tax solely because income was earned from interstate activity, and subjected interstate income to the risk of double taxation. *Wynne*, 135 S.Ct. at 1803.

¹⁹ See *Allied-Signal, Inc. v. Director, Div. of Taxation*, 504 U.S. 768 (1992) for a brief history of the unitary business principle.

²⁰ See *Allied-Signal*, 504 U.S. at 772-773. It is important to note that, in Iowa, this unitary business principle does not mandate combined reporting for businesses. For a discussion of combined reporting, see Part IV, Section C, Subsection 3, of the Legislative Guide entitled *State Taxation — Corporate Income Tax and Franchise Tax*, available at <https://www.legis.iowa.gov/publications/legalPubs/legisGuides> (last visited September 16, 2015).

²¹ Iowa Code §422.32(1)(I).

²² *Allied-Signal* at 783 (quoting *Container Corp. of America v. Franchise Tax Bd.*, 463 U.S. 159, 179 (1983)). See also *Super Valu Stores, Inc., v. Iowa Dept. of Revenue and Finance*, 479 N.W.2d 255 (1991) (holding subsidiary corporation to be part of unitary business because relationship produced “economies of scale and transfers of value,” thus sale of subsidiary was apportionable business income).

²³ Iowa Code §422.33(2)(a)(2)(c), (d); Iowa Admin. Code 701-54.5, 701-54.6. For a more in-depth discussion on the allocation and apportionment of corporate income in Iowa, see Part IV, Section B, Subsection 2, of the Legislative Guide entitled *State Taxation — Corporate Income Tax and Franchise Tax*, available at <https://www.legis.iowa.gov/publications/legalPubs/legisGuides> (last visited September 16, 2015). Iowa’s single-factor sales formula was challenged in *Moorman Manufacturing Co. v. Bair*, 437 U.S. 267 (1978), but was upheld by the Court. The Court noted that “states have wide latitude in the selection of apportionment formulas and that formula-produced assessment will only be disturbed when the taxpayer has proved by ‘clear and cogent evidence’ that the income attributed to the state is in fact ‘out of all appropriate proportions to the business transacted...in that state’...or has ‘led to a grossly distorted result.’” *Moorman*, 437 U.S. at 274.



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c. Discrimination Against Interstate Commerce. A state tax law may not discriminate against interstate commerce by imposing greater burdens on out-of-state goods, activities, or enterprises than on in-state goods, activities, or enterprises. Such discrimination occurs not only when a tax explicitly favors in-state commerce, but also when it has the economic effect of discrimination.²⁴

d. Fairly Related. A state tax law must be fairly related to the services provided by the state, but the Court has held that this is not a particularly high hurdle to overcome and does not require an intensive factual inquiry into the value of state benefits received by a taxpayer.²⁵ Instead, it only requires that the measure of the tax be reasonably related to the extent of the taxpayer's contact with the state.²⁶

2. State Taxation of Foreign Commerce

In an increasingly global economy, it becomes more likely that state tax law may burden foreign commerce. Given the federal government's need to "speak with one voice" in foreign affairs, the Supreme Court has strictly limited the states' power to tax foreign commerce. In addition to the four-part test described above, a state tax also must not cause international multiple taxation or "impair federal uniformity" in the area of foreign commerce.²⁷

The result is that, even more so than under the Interstate Commerce Clause, state tax laws must not discriminate against foreign commerce. When Iowa attempted to impose the state corporate income tax on the dividend income of foreign subsidiaries but not on the dividend income of subsidiaries based in the United States, the Supreme Court held that it was a burden on foreign commerce even though the tax did not specifically favor Iowa businesses. According to the court, discrimination against foreign commerce creates implications for the nation as a whole and, therefore, such decisions must be reserved to the federal government.²⁸

3. Exceptions to the Dormant Commerce Clause

If a tax is found to violate the dormant Commerce Clause, it may be saved under limited circumstances. The first such circumstance is if the tax is a "compensatory" or "complementary" tax meant to cure a comparable tax burden specific to in-state

²⁴ For examples of discriminatory taxes, see *Boston Stock Exchange v. State Tax Com.*, 429 U.S. 318 (1977) (invalidating transfer tax giving reduced rates to transfers occurring in New York through the New York Stock Exchange); *Bacchus Imports, Ltd. v. Dias*, 468 U.S. 263 (1984) (invalidating Hawaii liquor tax exemption for certain liquors that happened to be locally produced or made from locally grown fruit); *Armco Inc. v. Hardesty*, 467 U.S. 638 (1984) (invalidating West Virginia tax exemption for wholesalers who also engage in manufacturing activities in state); *Tyler Pipe Industries, Inc. v. Washington State Dept. of Revenue*, 483 U.S. 232 (1987) (invalidating Washington tax exemption for manufacturers who also engage in wholesaling activities in state); *New Energy Co. of Indiana v. Limbach*, 486 U.S. 269 (1988) (invalidating Ohio fuel tax credit for use of gasohol because credit was limited to gasohol produced in Ohio or in states that provided reciprocal tax advantages to Ohio-produced gasohol); *Westinghouse Electric Corp. v. Tully*, 466 U.S. 388 (1984) (invalidating New York franchise tax credit attributable only to receipts from exports shipped from New York); or *West Lynn Creamery, Inc. v. Healy*, 512 U.S. 186 (1994) (invalidating Massachusetts "premium payment" for all milk sold in-state where proceeds were earmarked for distribution only to Massachusetts' producers).

²⁵ See, for example, *Commonwealth Edison Co. v. Montana*, 453 U.S. 609 (1981) (upholding a 30 percent coal severance tax against a challenge that the value of services provided by the state were not quantitatively related to the tax paid).

²⁶ *Id.* at 625-626.

²⁷ *Japan Line, Ltd. v. County of Los Angeles*, 441 U.S. 434 (1979).

²⁸ *Kraft General Foods, Inc. v. Iowa Dept. of Revenue*, 505 U.S. 71 (1992).



commerce.²⁹ The classic example is the use tax, which applies to purchases outside of a state and used in state, because it complements the sales tax, which can only be applied to in-state purchases. “The tax serves the double purpose of producing revenue that otherwise might not be available, and of furnishing some measure of protection to Iowa dealers from competition with outside vendors not subject to liability for sales tax.”³⁰ The use tax might appear on its face to be a tax on goods purchased in another state and, if so, would seem to overreach the state’s taxing power under the dormant Commerce Clause. However, the Court has held that use taxes are valid as long as the burden on in-state purchases is the same as the burden on out-of-state purchases.³¹ Thus, Iowa imposes both its sales tax and use tax at the same rate and provides a credit against the use tax for sales tax paid in another state.³²

The tax may also be saved if it goes beyond regulation and is part of the state’s traditional government function. For example, a state is allowed to provide a tax exemption for its own bonds while disallowing the exemption for other states’ bonds because the issuance of debt to pay for public projects is a quintessentially public function.³³

4. Federal Law and the Commerce Clause

While the Supreme Court has often used the dormant aspect of the Commerce Clause to restrict state taxing powers, Congress is always free to legislate in this area and has done so. The Interstate Income Act of 1959, better known as Public Law No. 86-272 is one such instance. This law prohibits a state from imposing an income tax on an out-of-state corporation whose only business activities in the state are the solicitation of orders of tangible personal property that are approved and filled outside the state.³⁴ The law was enacted in response to a 1959 U.S. Supreme Court decision in which the imposition of the Minnesota income tax was upheld against an Iowa corporation that had a sales office and several salesmen in Minnesota for the purpose of soliciting sales from Minnesota customers to be approved and filled in Iowa.³⁵

²⁹ A tax must satisfy a three-prong inquiry to be considered a valid compensatory tax: 1) the state must identify the intrastate tax burden for which it is attempting to compensate; 2) the tax on interstate commerce must be shown to roughly approximate — but not exceed — the amount of the tax on intrastate commerce; and 3) the events on which the interstate and intrastate taxes are imposed must be substantially equivalent. *Oregon Waste Systems Inc. v. Dept. of Environmental Quality*, 511 U.S. 93 (1994). This is historically a very difficult inquiry to satisfy.

³⁰ *Sturtz v. Iowa Department of Revenue*, 373 N.W.2d 131, 133 (Iowa 1985) (quoting *Dain Manufacturing Co. v. Iowa State Tax Comm’n*, 22 N.W.2d 786, 788 (Iowa 1946).

³¹ *Henneford v. Silas Mason Co.*, 300 U.S. 577 (1937).

³² Iowa Code §§423.2, 423.5, 423.22.

³³ *Department of Revenue of Ky. v. Davis*, 553 U.S. 328, 341-342 (2008).

³⁴ 15 U.S.C. §381 et seq. “Solicitation of orders” encompasses solicitation by a corporation’s employees or solicitation by an independent contractor, including an independent contractor who maintains an office in the state related to the solicitation of sales.

³⁵ *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450 (1959). In enacting Public Law No. 86-272, Congress was concerned that “persons engaged in interstate commerce are in doubt as to the amount of local activities within a State that will be regarded as forming a sufficient...connection with the State to support the imposition of a tax on net income from interstate operations and ‘properly apportioned’ to the State.” *Wisconsin Dept. of Revenue v. William Wrigley, Jr. Co.*, 505 U.S. 214, 222 (quoting S. Rep. No. 658, 86th Cong., 1st Sess., pp. 2-3 (1959)).



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In Iowa, “solicitation of orders” includes activities that explicitly or implicitly propose a sale or that are entirely ancillary to requests for purchases. An activity is not entirely ancillary if it serves an independent business function apart from the solicitation of orders, or if the corporation has reason to perform it regardless of the sale.³⁶

It is important to note that the law only applies to taxes on, or measured by, net income, and to sales of tangible personal property. In today’s economy, however, much interstate commercial activity involves the sale of services and other intangible forms of property not embraced by the term “tangible personal property.”

Another example is the McCarran-Ferguson Act of 1945, which exempts the insurance business from several forms of federal regulation, and declares that “silence on the part of Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States.”³⁷ The law was enacted in response to a 1944 U.S. Supreme Court decision which held that the business of insurance was commerce and subject to the Commerce Clause.³⁸ The law has the effect of removing Commerce Clause restrictions on states’ power to tax the insurance business.³⁹ This has led most states, including Iowa, to enact so-called “retaliatory” taxes on out-of-state insurance companies in order to discourage other states from imposing higher taxes on a state’s domestic insurers.⁴⁰ These taxes are usually structured as an additional tax levied on insurance companies domiciled outside a taxing state if such insurance company’s home state imposes higher taxes on similar nondomiciled insurance companies.

Finally, in recent years there has been considerable interest by public and private stakeholders in passing federal legislation that will allow state governments to require out-of-state retailers to collect sales and use tax on purchases shipped to that state, thereby abrogating the requirement established in *Quill v. North Dakota*, discussed above, that a retailer have physical presence in the state in order to create substantial

³⁶ Iowa Admin. Code 701-52.1(3). Examples of activities that are not entirely ancillary include repair, installation, service-type activities, or collection on accounts. The Department of Revenue maintains nonexhaustive lists of activities that do and do not qualify for protection under Public Law No. 86-272. Iowa Admin. Code 701-52.1(2)(a), 701-52.1(3). See also *Wrigley*, 505 U.S. 214, in which the U.S. Supreme Court held that an Illinois chewing gum manufacturer’s activities in Wisconsin were “entirely ancillary” when it recruited and trained employees and used hotels and homes for sales meetings, but were not “entirely ancillary” when it supplied and sold gum to retailers who agreed to install display racks, and stored gum for these purposes within Wisconsin. However, it should be noted that activities that are sufficiently de minimis, and unrelated to the solicitation of orders, will not destroy a corporation’s protection from income tax under Public Law No. 86-272. Activities are sufficiently de minimis if they establish only a trivial additional connection to the taxing state. *Wrigley* at 231-232.

³⁷ 15 U.S.C. §1011 et seq.

³⁸ See *United States v. South-Eastern Underwriters Association*, 322 U.S. 533 (1944).

³⁹ See *Western and Southern Life Ins. Co. v. State Bd. of Equalization of California*, 451 U.S. 648, 652-653 (1981) (upholding California’s retaliatory insurance tax).

⁴⁰ See Part III, Section B, Subsection 5, of this Guide for a discussion of Iowa’s retaliatory insurance tax.



nexus.⁴¹ Although several bills have been introduced, nothing has passed at the time of this Guide's publication.⁴²

B. The Due Process Clause⁴³

A state's power to tax is also subject to the limitations of the Due Process Clause. An attempt by a state to collect a tax from a taxpayer is an exercise of the state's jurisdiction over that taxpayer. In exercising such jurisdiction, states are constrained by the fairness concerns central to the Due Process Clause. The primary inquiry in this context is, given the extent and nature of the taxpayer's connections to the state, whether the taxpayer should reasonably expect to be subject to that jurisdiction.

The Supreme Court has held that as long as there is "some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax", the requirements of the Due Process Clause are satisfied.⁴⁴ However, because of the different nexus requirements of the Commerce Clause and the Due Process Clause, it is possible to have a connection that is sufficient to satisfy due process but that is, at the same time, insufficient to justify its impact on interstate commerce. From a practical perspective, then, states seeking to exercise their taxing power generally need to be more concerned with Commerce Clause nexus than Due Process Clause nexus.

C. The Equal Protection Clause⁴⁵

Another constitutional limitation on a state's power to tax is the Equal Protection Clause. In general, the Equal Protection Clause ensures that everyone has the same rights under the law.

The Equal Protection Clause does not, however, ensure that everyone pays the same amount of taxes. For example, the Supreme Court has held that:

[T]he States, in the exercise of their taxing power, are subject to the requirements of the Equal Protection Clause of the Fourteenth Amendment. But that clause imposes no iron rule of equality...The State may impose different specific taxes upon different trades and professions and may vary the rate of excise upon various products. It is not required to resort to close distinctions or to maintain a precise, scientific uniformity with reference to composition, use or value.⁴⁶

The Court has also given states substantial flexibility to create tax classifications, holding that "where taxation is concerned..., the States have large leeway in making

⁴¹ This desire to lower the physical presence requirement of *Quill* led, in part, to the creation of the Streamlined Sales and Use Tax Agreement, which is discussed in detail in Part IV of the Legislative Guide entitled *State Taxation — Sales and Use Taxes*, available at <https://www.legis.iowa.gov/publications/legalPubs/legisGuides> (last visited September 23, 2015).

⁴² See, for examples, the 2011 Mainstreet Fairness Act (S. 1452, H.R. 2701); the 2011 Marketplace Fairness Act (S. 1832); the 2011 Marketplace Equity Act (H.R. 3179); the 2013 Marketplace Fairness Act (H.R. 684, S. 743); the 2013 Marketplace and Internet Tax Fairness Act (S. 2609); the 2015 Marketplace Fairness Act (S. 698); and the 2015 Remote Transactions Parity Act (H.R. 2775).

⁴³ No state may "deprive any person of life, liberty, or property without due process of law." U. S. Const. amend. XIV, §1.

⁴⁴ *Miller Bros. Co. v. Maryland*, 347 U.S. 340, 344-345 (1954).

⁴⁵ No state may "deny to any person within its jurisdiction the equal protection of the laws." U. S. Const. amend. XIV, §1.

⁴⁶ *Allied Stores of Ohio, Inc. v. Bowers*, 358 U.S. 522, 526-527 (1959).



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classifications and drawing lines which in their judgment produce reasonable systems of taxation.”⁴⁷

In light of the substantial leeway allowed states in exercising their powers of taxation, the Supreme Court has implied that, with few exceptions, only taxes that affect “a fundamental interest” or contain “a classification based on a suspect criterion” such as race or gender are in danger of invalidation under the Equal Protection Clause.⁴⁸

As long as there is a legitimate purpose and as long as the classifications created are rationally related to that purpose, a state tax will not violate the Equal Protection Clause. Thus, when the Iowa Supreme Court held unconstitutional a state statute⁴⁹ that taxed racetrack slot machine revenues at a different rate from riverboat slot machine revenues, the United States Supreme Court unanimously overturned the ruling, upholding the Iowa General Assembly’s decision to tax riverboats and racetracks differently.⁵⁰

D. The Import-Export Clause⁵¹ and the Duty-of-Tonnage Clause⁵²

The Commerce Clause, the Due Process Clause, and the Equal Protection Clause are obviously not confined to questions of taxation, and disputes over their proper interpretation embrace some of the most difficult issues in federal constitutional law. The Import-Export Clause and the Duty-of-Tonnage Clause, however, are expressly concerned with state taxation. Perhaps because they have the virtues of narrower scope and clearer meaning, these clauses have generated fewer cases and controversies. Yet despite their relatively low constitutional profile, they too represent important curbs on state taxing powers.

1. The Import-Export Clause

The Import-Export Clause prohibits states from laying “imposts or duties on imports or exports except what may be absolutely necessary for executing its inspection laws.” Until the 1970s, whether a shipment of goods enjoyed the protection of this clause depended on whether the goods were properly considered imports or exports.⁵³

Since the 1970s, however, the application of the clause has been determined by examining the nature of the state tax at issue rather than the character of the goods. Today, a state may, for example, levy an *ad valorem* property tax on imported goods as long as it is clear that the tax does not create “special protective tariffs or particular

⁴⁷ Lehnhausen v. Lake Shore Auto Parts Co., 410 U.S. 356, 359 (1973).

⁴⁸ Exxon Corp. v. Eagerton, 462 U.S. 176, 195 (1983). See also Minnesota v. Clover Leaf Creamery Co., 449 U.S. 456 (1981).

⁴⁹ See generally Iowa Code ch. 99F.

⁵⁰ Fitzgerald v. Racing Ass’n of Central Iowa, 539 U.S. 103 (2003). The ruling from the United States Supreme Court was limited in application to the federal Equal Protection Clause. The Iowa Supreme Court once again struck the statute down on remand, but this subsequent decision was based solely on the Iowa Constitution. See Racing Ass’n Of Central Iowa v. Fitzgerald, 675 N.W.2d 1 (Iowa 2004).

⁵¹ “No state shall, without the consent of Congress, lay any imposts or duties on imports or exports, except what may be absolutely necessary for executing its inspection laws; and the net produce of all duties and imposts laid by any state on imports or exports shall be for the use of the treasury of the United States; and all such laws shall be subject to the revision and controul [sic] of the Congress.” U.S. Const. art. I, §10, cl. 2.

⁵² “No state shall, without the consent of Congress, lay any duty of tonnage.” U.S. Const. art. I, §10, cl. 3.

⁵³ See Michelin Tire Corp. v. Wages, 423 U.S. 276 (1976); Dept. of Revenue v. Association of Washington Stevedoring Cos., 435 U.S. 734 (1978).



preferences for certain domestic goods” and as long as the levy does not “encourage or discourage any importation in a manner inconsistent with federal regulation.”⁵⁴

In other words, as it has with the Commerce Clause, the Supreme Court has reinterpreted the Import-Export Clause, viewing it not as a blanket immunity from state taxation but as a prohibition on discriminatory taxation and an injunction against interference with federal trade policy.

2. The Duty-of-Tonnage Clause

The Duty-of-Tonnage Clause prohibits states from imposing a tax on shipping or on the flow of goods through a port. The Supreme Court has noted that the intent of the Duty-of-Tonnage Clause “mirrors” that of the Import-Export Clause, both of which seek “to prevent states with ‘convenient ports’ from placing other states at an economic disadvantage by laying levies that would tax the consumption of their neighbors.”⁵⁵

Furthermore, the clause has been interpreted to embrace “all taxes and duties regardless of their name or form, and even though not measured by the tonnage of the vessel, which operate to impose a charge for the privilege of entering, trading in, or lying in a port.”⁵⁶ In other words, a state cannot circumvent the Import-Export Clause restriction merely by levying a tax on a ship’s carrying capacity instead of on the goods it carries.

However, the Duty-of-Tonnage Clause does not restrict a state or a municipality from charging fees for the provision of port services. For example, when the City of Keokuk, which had an exclusive right from the state of Iowa to levy “wharfage” fees on Mississippi River shipping, sought to collect such fees from interstate commercial shippers using the city’s wharves, the Supreme Court upheld the arrangement, noting that “a charge for services rendered or for conveniences provided is in no sense a tax or a duty.”⁵⁷

E. The Supremacy Clause⁵⁸

Another federal constitutional limitation on state taxation is the Supremacy Clause, which provides that the laws of the United States are “the supreme law of the land.” Since 1819, this clause has been interpreted to give the federal government unqualified immunity from state taxation.⁵⁹ However, the immunity applies only to the government itself and not to its contractors.⁶⁰

⁵⁴ *Michelin Tire Corp. v. Wages*, 423 U.S. 276, 286 (1976).

⁵⁵ *Polar Tankers, Inc. v. City of Valdez*, 129 S. Ct. 2277 (2009).

⁵⁶ *Clyde Mallory Lines v. Alabama*, 296 U.S. 261, 265-266 (1935).

⁵⁷ *Packet Company v. Keokuk*, 95 U.S. 80 (1877).

⁵⁸ The laws of the United States “shall be the supreme law of the land.” U.S. Const. art. VI, sec. 2.

⁵⁹ *M’Culloch v. Maryland*, 17 U.S. 316 (1819).

⁶⁰ *United States v. New Mexico*, 455 U.S. 720 (1982).



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F. The First Amendment⁶¹

The final federal constitutional limitation on state taxing powers to be aware of is the First Amendment. As with many state laws, it is possible for a tax to violate the First Amendment, particularly if the tax is directed at the content of speech,⁶² the exercise of religion,⁶³ or a certain segment of the media.⁶⁴ However, in general, state taxes more often implicate issues of fairness or state power than issues of speech, association, or religion.

III. Taxes Imposed or Administered by the State of Iowa

The federal limitations discussed above nonetheless still leave states substantial leeway to design their tax systems in ways they deem appropriate. In many states, including Iowa, this has resulted in a variety of different taxes. In summarizing these taxes for purposes of a general overview, it is helpful to group them into categories and discuss some of their general similarities as well as to highlight some of the particular details of their implementation under Iowa law.

A. Income Taxes

An income tax refers to a tax levied against a taxpayer's income. The amount of tax due is typically calculated as a certain percentage of that income. Thus, in determining tax liability, much depends on how "income" is defined and calculated.

Generally speaking, "income," in the case of individuals, means total earnings, including wages, salary, profits, interest payments, and rent received. "Income" in the case of business entities generally means "net profit" which is calculated by subtracting expenses from revenues. For both individuals and business entities, the amount of income is measured over a certain period of time (e.g., calendar year, fiscal year).

1. The Individual Income Tax⁶⁵

Iowa imposes an individual income tax on the income of natural persons⁶⁶ and estates and trusts.⁶⁷ In addition, because the income of certain business entities is allowed to "pass through" to the individual owners for purposes of taxation, the tax base of the individual income tax embraces the profits of those businesses.

The tax is imposed on the amount of an individual's "taxable income."⁶⁸ The computation of taxable income for Iowa purposes is, in concept, relatively simple. The starting point is the taxpayer's federal adjusted gross income (AGI) which is then

⁶¹ "Congress shall make no law respecting an establishment of religion, or prohibiting the free exercise thereof; or abridging the freedom of speech, or of the press; or the right of the people peaceably to assemble, and to petition the Government for a redress of grievances." U.S. Const. amend. I.

⁶² *Arkansas Writer's Project Inc. v. Ragland*, 481 U.S. 221 (1987).

⁶³ *Jimmy Swaggart Ministries v. Bd. of Equalization*, 493 U.S. 378 (1990).

⁶⁴ *Leathers v. Medlock*, 499 U.S. 439 (1991).

⁶⁵ Iowa Code ch. 422, div. II.

⁶⁶ Iowa Code §422.5 imposes the tax on the taxable income of "every resident and nonresident of the state" but §422.4 makes clear that "resident" and "nonresident" only apply to individuals.

⁶⁷ Iowa Code §422.6.

⁶⁸ Iowa Code §422.5(1).



modified by certain Iowa statutory adjustments⁶⁹ to arrive at the taxpayer's "net income."⁷⁰ Net income is in turn adjusted by either a "standard deduction" or by the applicable "itemized deductions"⁷¹ to arrive at the amount of "taxable income."⁷² Taxable income is subject to tax according to nine progressive tax brackets starting at 0.36 percent on the first \$1,554 of taxable income, up to 8.98 percent on taxable income exceeding \$69,930.⁷³ Numerous credits are available against the individual income tax.⁷⁴

Both residents and nonresidents may be liable for Iowa's income tax.⁷⁵ In the case of residents, both income earned in Iowa and income earned in another state are subject to the tax, although, in order to avoid double taxation, a credit is provided for a resident's out-of-state income to the extent that income taxes have already been paid in the other state.⁷⁶ In the case of nonresidents, only that portion of income derived from Iowa sources is subject to the tax.⁷⁷

In Iowa, income taxes due on wages and other income⁷⁸ subject to the tax are required to be withheld at the source by employers and withholding agents who are subject to similar requirements for federal income tax collection purposes. While this withholding requirement is often referred to as a "withholding tax," it is technically not a separately imposed tax but rather the prepayment of individual income taxes according to calendar year estimates prepared by the Department of Revenue. Both residents and nonresidents subject to the individual income tax may be subject to these withholding requirements.⁷⁹ For a detailed discussion of the Iowa individual

⁶⁹ The term "adjustments" has been used in this context to reflect the fact that some of the Iowa-specific provisions adjust federal AGI "up" while others adjust it "down."

⁷⁰ Iowa Code §422.7. Deductions from federal AGI used to arrive at net income are sometimes referred to as "above-the-line" deductions. These deductions may be Iowa specific. For example, Iowa law provides a deduction for federal income tax paid.

⁷¹ Iowa Code §422.9. Deductions from net income used to arrive at taxable income are sometimes referred to as "below-the-line" deductions. For the most part, the itemized deductions available for Iowa purposes are the same as those available under the Internal Revenue Code, but, as with the above-the-line adjustments to federal AGI, there are some Iowa statutory adjustments in addition to the list of federal itemized deductions. See Iowa Code §422.9(2).

⁷² Iowa Code §422.4(16). Note, however, that the final tax liability may be even further adjusted by any tax credits for which the taxpayer is eligible. However, such adjustments are made after the applicable rate bracket is applied to the taxable income.

⁷³ <https://tax.iowa.gov/press-release/iowa-department-revenue-announces-interest-rates-standard-deduction-amounts-and-tax> (last visited November 17, 2015).

⁷⁴ Iowa Code §§422.10-422.12C.

⁷⁵ For information on the propriety of taxing the income of out-of-state residents, see the discussion of the constitutional limitations on state taxation in Part II of this Guide.

⁷⁶ Iowa Code §422.8. See also Wynne, 135 S.Ct. 1787, discussed at note 18.

⁷⁷ Iowa Code §422.8. Many other states have income tax laws that, like Iowa's, allow for the taxation of the income of nonresidents. Since 2002, the Director of the Iowa Department of Revenue has had the authority, subject to approval by the General Assembly and the Governor, to make a reciprocal agreement with another state whereby each state agrees to exempt residents of the other state from payment of the first state's income tax. However, to date, the only agreement Iowa has made is with the state of Illinois.

⁷⁸ "Other income" includes winnings from pari-mutuel wagering and gambling games, and state tax is authorized to be withheld from such winnings at the source. See Iowa Code §§99D.16, 99F.18, 422.16(1)(d).

⁷⁹ Iowa Code §422.16.



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income tax, see the Legislative Guide entitled State Taxation: Individual Income Tax, available at <https://www.legis.iowa.gov/publications/legalPubs/legisGuides>.

2. The Corporate Income Tax⁸⁰

The corporate income tax is imposed on most for-profit corporations doing business in this state, or deriving income from sources within this state, including joint stock companies, associations organized for pecuniary profit, and partnerships and certain limited liability companies taxed as corporations under the Internal Revenue Code.⁸¹ The corporate income tax is not imposed on financial institutions or on insurance companies, both of which are subject to dedicated taxes structured specially for those types of businesses, nor is the tax imposed on nonprofit organizations exempt from federal income tax under section 501 of the Internal Revenue Code.⁸² However, such exempt nonprofit organizations are subject to Iowa corporate income tax on unrelated business income.⁸³

As with the individual income tax, the corporate income tax is linked to the federal tax code. The starting point for computing income for Iowa purposes is a corporation's federal taxable income. Certain Iowa statutory adjustments are made to the federal taxable income in order to arrive at a corporation's "net income" for Iowa tax purposes.⁸⁴

From there, the net income must be allocated and apportioned among Iowa and the other states in which the corporation does business, if any.⁸⁵ The resulting Iowa taxable income is then taxed at 6 percent on the first \$25,000; 8 percent on the next \$75,000; 10 percent on the next \$150,000; and 12 percent on Iowa taxable income of \$250,000 or more.⁸⁶ Numerous credits are available against the corporate income tax.⁸⁷

A detailed discussion of the Iowa corporate income tax may be found in the Legislative Guide entitled State Taxation — Corporate Income Tax and Franchise Tax, available at <https://www.legis.iowa.gov/publications/legalPubs/legisGuides> (last visited September 23, 2015).

B. Franchise and Insurance Taxes

1. The Franchise Tax on Financial Institutions⁸⁸

Technically speaking, a franchise tax is a tax levied on a company for the privilege of doing business in the state. In this respect, a franchise tax is distinct from

⁸⁰ Iowa Code §§422.32-422.41, 422.85-422.93.

⁸¹ Iowa Code §§422.32(1)(d), 422.33(1).

⁸² Iowa Code §422.34.

⁸³ Iowa Code §422.33(1A).

⁸⁴ Iowa Code §422.35.

⁸⁵ Iowa Code §§422.33(2), (3). Allocation and apportionment of a multi-state corporation can be especially complex because of the federal constitutional requirement of "fair apportionment," discussed in detail in Part II, Section A, Subsection 1, of this Guide.

⁸⁶ Iowa Code §422.33(1).

⁸⁷ Iowa Code §§422.33(5)-(30).

⁸⁸ See generally Iowa Code ch. 422, div. V.



an income tax. However, as with income taxes, the amount of franchise tax due must be determined in a way that fairly reflects the amount of activity attributable to the state, which is why a franchise tax may be imposed “according to and measured by” some measure of income in the state. As a practical matter, then, a franchise tax is closely akin to an income tax despite not technically being levied against income.

Iowa’s franchise tax is imposed only on financial institutions, which includes state banks, national banking associations, trust companies, federally and state-chartered savings and loan associations, financial institutions chartered by the Federal Home Loan Bank Board, and production credit associations.⁸⁹ It does not apply to credit unions, which are subject to the moneys and credits tax.⁹⁰

The franchise tax is levied “according to and measured by net income.” The computation of net income for a financial institution is substantially similar to computing net income for corporate income tax purposes, with a few adjustments.⁹¹ The tax is due annually in an amount equal to 5 percent of the institution’s net income earned in Iowa, as computed for purposes of the franchise tax.⁹² A detailed discussion of the Iowa franchise tax may be found in the Legislative Guide entitled *State Taxation — Corporate Income Tax and Franchise Tax*, available at <https://www.legis.iowa.gov/publications/legalPubs/legisGuides> (last visited September 23, 2015).

2. The Moneys and Credits Tax on Credit Unions

Under Iowa law, credit unions are deemed institutions for savings, rather than financial institutions, and are subject to the moneys and credits tax.⁹³ The moneys and credits tax is neither a tax on net income nor a tax measured by net income as with the franchise tax. Instead, state credit unions are required to hold a certain percentage of their income in reserve to cover losses and defaults,⁹⁴ and the moneys and credits tax is imposed at the rate of one-half cent on each dollar of these reserves after subtracting an annual exemption amount of \$40,000.⁹⁵ Thus, the moneys and credits tax is not tied to a credit union’s profitability but rather to the value of its deposits. Several tax credits are available against the moneys and credits tax, including:⁹⁶

- Credit for certain sales tax paid by third-party developers.⁹⁷

⁸⁹ Iowa Code §§422.60(1), 422.61(1).

⁹⁰ Iowa Code §533.329.

⁹¹ Iowa Code §422.61(3). Most of the adjustments relate to the treatment of income from government securities. Although states are generally prohibited from taxing federal securities, an exception exists for a nondiscriminatory franchise tax. See 31 U.S.C. §3124(a)(1).

⁹² Iowa Code §422.63.

⁹³ Iowa Code §533.329.

⁹⁴ Iowa Code §533.303.

⁹⁵ Iowa Code §533.329(2)(a).

⁹⁶ For descriptions of these tax credits, please see Part IV, Section B, Subsection 4, of the Legislative Guide entitled *State Taxation — Corporate Income Tax and Franchise Tax*, available at <https://www.legis.iowa.gov/publications/legalPubs/legisGuides> (last visited September 24, 2015).

⁹⁷ Iowa Code §§15.331C, 533.329(2)(d).



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- Investment tax credits.⁹⁸
- Iowa fund of funds tax credit.⁹⁹
- Endow Iowa tax credit.¹⁰⁰
- Redevelopment tax credits.¹⁰¹
- Innovation fund investment tax credit.¹⁰²
- Workforce housing investment tax credit.¹⁰³
- Solar energy system tax credit.¹⁰⁴

The money and credits tax is levied by the board of supervisors and collected by the county treasurer at the location of the credit union as shown in its articles of incorporation.¹⁰⁵ Tax revenues collected from credit unions incorporated inside a city are apportioned 20 percent to the county, 30 percent to the city, and 50 percent to the General Fund of the State.¹⁰⁶ Tax revenues collected from credit unions incorporated outside a city are apportioned 50 percent to the county, and 50 percent to the State General Fund.¹⁰⁷

3. The Gross Premiums Tax on Insurance Companies

The insurance companies taxes are neither an income tax nor a tax measured by income. Since they are generally imposed on the value of premiums received, the tax is due regardless of whether the insurance company realizes a profit. In this respect, the tax resembles a gross receipts tax, or even a sales tax, more so than an income tax.

The insurance companies tax is imposed on “every insurance company or association of whatever kind or character” except fraternal benefit associations, and on mutual service corporations.¹⁰⁸

For life insurance companies or associations, the tax is equal to 1 percent of the gross premiums received on risks resident in Iowa, excluding premiums from policies or contracts issued in connection with a pension, annuity, profit-sharing plan or individual retirement annuity exempt under specified federal Internal Revenue Code sections, and excluding all consideration received in connection with an annuity

⁹⁸ Iowa Code §§15.333, 15E.43, 533.329(2)(e), (f).

⁹⁹ Iowa Code §§15E.66, 533.329(2)(g).

¹⁰⁰ Iowa Code §§15E.305, 533.329(2)(h).

¹⁰¹ Iowa Code §§15.291-295, 533.329(2)(i).

¹⁰² Iowa Code §§15E.52, 533.329(2)(j).

¹⁰³ Iowa Code §§15.355(3), 533.329(2)(k).

¹⁰⁴ Iowa Code §§422.11L, 533.329(2)(l).

¹⁰⁵ Iowa Code §533.329(2)(a), (c).

¹⁰⁶ Iowa Code §533.329(2)(b).

¹⁰⁷ Iowa Code §533.329(2)(b).

¹⁰⁸ Iowa Code §§135.120, 432.1, 432.2, 518.18, 518A.35.



contract.¹⁰⁹ Also excluded are certain premiums returned or dividends paid to policyholders.¹¹⁰

For other insurance companies and associations, the tax is equal to 1 percent of the gross premiums written, and assessments and fees received, for business done in Iowa, including insurance on property situated in Iowa or, in the case of surplus lines insurance, for policies where the home state of the insured is Iowa.¹¹¹ Excluded are amounts returned on canceled or rejected policies, and amounts received in connection with ocean marine insurance subject to the marine insurance tax.¹¹²

For mutual service corporations, the tax is equal to 1 percent of the gross amount of payments received for subscriber contracts covering Iowa residents, excluding amounts returned upon canceled or rejected contracts.¹¹³

For county mutual insurance associations, the tax is equal to 1 percent of the gross premiums received, excluding amounts returned for canceled or rejected policies, and excluding premiums paid for windstorm or hail reinsurance on property specifically reinsured, but not excluding reinsurance premiums received by a reinsurer upon such risks.¹¹⁴

For state mutual insurance associations, the tax is equal to 1 percent of gross receipts from premiums and fees for business done in Iowa, including insurance on property situated in Iowa, but excluding amounts received or paid for reinsurance.¹¹⁵ However, a state mutual insurance association is required to include amounts for reinsurance of windstorm or hail risks written by county mutual insurance associations after deducting amounts returned as dividends or on canceled or rejected policies on property situated in Iowa.¹¹⁶

Premiums collected by participating insurers under the hawk-i Program and for benefits acquired on behalf of state employees by the Department of Administrative Services or the state Board of Regents are exempt from the insurance companies tax.¹¹⁷

Several tax credits are available against the insurance companies tax, including:¹¹⁸

- Historic preservation and cultural and entertainment district tax credit.¹¹⁹

¹⁰⁹ Iowa Code §432.1(1), (2).

¹¹⁰ Iowa Code §432.1(1)(b), (c).

¹¹¹ Iowa Code §432.1(3).

¹¹² Iowa Code §432.1(3). See Subsection 4 of this Section B for a description of the marine insurance tax.

¹¹³ Iowa Code §432.2. A mutual service corporation is, broadly speaking, a corporation organized under Iowa Code ch. 514 for the purpose of operating plans for a nonprofit hospital service, health care service, or pharmaceutical or optometric service, to subscribers. See Iowa Code §514.1.

¹¹⁴ Iowa Code §518.18.

¹¹⁵ Iowa Code §518A.35(1).

¹¹⁶ Iowa Code §518A.35(1).

¹¹⁷ Iowa Code §432.13.

¹¹⁸ For descriptions of these tax credits, see Part IV, Section B, Subsection 4, of the Legislative Guide entitled State Taxation — Corporate Income Tax and Franchise Tax, available at <https://www.legis.iowa.gov/publications/legalPubs/legisGuides> (last visited September 24, 2015).



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- Investment tax credits.¹²⁰
- Endow Iowa tax credit.¹²¹
- Tax credits for wind energy production and renewable energy.¹²²
- Workforce housing investment tax credit.¹²³
- Credit for certain sales tax paid by third-party developers.¹²⁴
- Iowa fund of funds tax credit.¹²⁵
- Redevelopment tax credits.¹²⁶
- Innovation fund investment tax credit.¹²⁷

If an insurance company had tax liability in the prior year of at least \$1,000, prepayment of taxes in two equal installments is required. The first installment, equal to 50 percent of the prior year's taxes, is due by June 1. The second installment, also equal to 50 percent of the prior year's taxes, is due by August 15.¹²⁸

4. The Marine Insurance Tax

The marine insurance tax, while also a tax on insurance companies, is somewhat different from the gross premiums tax because it is a tax on a particular type of insurance, and because it more closely resembles a tax on income.

Insurers selling marine insurance in Iowa are, with respect to that marine insurance, subject to the marine insurance tax in lieu of the regular insurance companies tax discussed above.¹²⁹ The tax is imposed at a rate of 6.5 percent of the "taxable underwriting profit" on ocean marine insurance written in Iowa.¹³⁰ The underwriting profit for marine insurance written within Iowa is the proportion of the total underwriting profit for marine insurance which the amount of net premiums written within Iowa bears to the total amount of net premiums.¹³¹ The taxable underwriting profit is essentially the amount of net marine insurance premiums earned less specified losses and expenses incurred that relate to the marine insurance business, and is calculated as a three-year average.¹³²

¹¹⁹ Iowa Code §§404A.2, 432.12.

¹²⁰ Iowa Code §§15.333A, 15E.43, 432.12C.

¹²¹ Iowa Code §§15E.305, 432.12D.

¹²² Iowa Code §432.12E; Iowa Code ch. 476B, 476C.

¹²³ Iowa Code §§15.355(3), 432.12G.

¹²⁴ Iowa Code §§15.331C, 432.12H.

¹²⁵ Iowa Code §§15E.66, 432.12I.

¹²⁶ Iowa Code §§15.291-15.295, 432.12L.

¹²⁷ Iowa Code §§15E.52, 432.12M.

¹²⁸ Iowa Code §§432.1(6), 518.18(3), 518A.35(3).

¹²⁹ Iowa Code §§432A.1, 432A.9.

¹³⁰ Iowa Code §432A.1.

¹³¹ Iowa Code §432A.2.

¹³² Iowa Code §§432A.3-432A.6.



5. The Reciprocal Tax on Foreign Insurance Companies

The state of Iowa imposes an additional reciprocal tax on foreign insurance companies doing business in Iowa whose domiciliary state imposes a greater tax on Iowa companies than Iowa does on the foreign companies.¹³³ Authority for this reciprocal tax provides that when in another state, the premium, income, or other taxes and fees on Iowa insurance companies exceed those same state taxes and fees imposed by Iowa on that state's insurance companies, then Iowa will impose the higher amount of taxes and fees on that state's insurance companies. The reciprocal taxes do not apply to personal property taxes or individual income taxes.¹³⁴

C. Retail Sales and Use Taxes

A retail sales tax is typically levied as a percentage of the sales price of a transaction and is collected by the seller at the point of sale. A use tax is closely related to a sales tax, and the two taxes are usually implemented as complements to each other.¹³⁵ A use tax is typically levied as a percentage of the purchase price of property or a service purchased outside the state but used in the state, and is paid by the user or under certain circumstances collected by the seller at the point of sale.

The Iowa state sales tax is imposed at a rate of 6 percent on the sales price of all sales of tangible personal property and from the furnishing of enumerated services sold at retail in this state to the ultimate consumer or user of the property or services.¹³⁶ The Iowa use tax is imposed at a rate of 6 percent on the purchase price of all tangible personal property or enumerated services sold for use in Iowa and used in Iowa.¹³⁷ To avoid constitutional issues of double taxation, the Iowa use tax exempts any property or service upon which the Iowa sales tax has been paid, and offers a credit for sales or use taxes paid in another state on the same good or service.¹³⁸ Numerous other exemptions from the sales and use tax are provided.¹³⁹ A detailed discussion of the Iowa sales and use tax may be found in the Legislative Guide entitled *State Taxation — Sales and Use Taxes*, available at <https://www.legis.iowa.gov/publications/legalPubs/legisGuides> (last visited September 25, 2015).

D. Special Excise Taxes

The term “excise tax” is somewhat vague and not susceptible to a precise, universal meaning. Sales taxes are often considered “excise taxes” because they are taxes on consumption and are levied on a single event (i.e., a commercial transaction). Similarly, use taxes are levied on the single event of “use” in the state. But these taxes apply to a

¹³³ See Part II, Section A, Subsection 4, of this Guide for a discussion on the history of, and constitutional authority for, retaliatory insurance taxes.

¹³⁴ Iowa Code §505.14.

¹³⁵ For more information on the complementary nature of sales and use taxes, see “Exceptions to the Dormant Commerce Clause” in Part II, Section A, Subsection 3, of this Guide.

¹³⁶ Iowa Code §423.2(1)-(9). A local option sales tax may also be imposed by local governments at a rate not to exceed 1 percent. Thus, the maximum combined state and local sales tax rate cannot exceed 7 percent. See Section F, Subsection 1, below, for a discussion of the local option sales and use tax.

¹³⁷ Iowa Code §423.5.

¹³⁸ Iowa Code §§423.6(1), 423.22.

¹³⁹ Iowa Code §§423.3, 423.6.



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broad range of products and services. Taxes traditionally thought of as excise taxes tend to have one or more of the following characteristics in common.

First, an excise tax is usually very specific, often targeting a particular type of transaction or class of goods, such as taxes on gasoline, alcohol, or cigarettes. Second, excise taxes are often levied at a fixed amount per unit of measurement, rather than as a proportional value. For example, gasoline is often taxed per gallon, beer per barrel, and tobacco per cigarette. Sales and use taxes, on the other hand, are levied as a proportion of the transaction cost. Finally, certain excise taxes may be accompanied by social disapprobation and may bear high levy rates intended to not only raise revenue but to reduce consumption. These are often colloquially referred to as “sin taxes.”

Iowa has a number of taxes that could be considered special excise taxes. Some, like the taxes on alcohol and cigarettes, exhibit all the characteristics described above. Others, like the hotel and motel tax or the construction equipment tax, may only exhibit the characteristic of being specifically targeted.

1. The State Hotel and Motel Tax¹⁴⁰

Hotel and motel room rentals were once taxed under the sales tax, but were removed from the sales tax base in order to maintain a uniform tax base for the sales and use taxes. Hotel and motel room rentals are now subject to a special excise tax and are exempt from the sales and use tax.

The hotel and motel tax is imposed at a rate of 5 percent on the sales price from the renting in Iowa of any room, apartment, or sleeping quarters in a hotel, motel, inn, public lodging house, rooming house, or manufactured or mobile home which is tangible personal property, or in a tourist court, or in any place where sleeping accommodations are furnished to transient guests for rent, whether with or without meals.¹⁴¹ However, the tax is not imposed on the renting of such accommodations if rented to the same person for more than 31 consecutive days, or on the renting of rooms in dormitories and memorial unions at Iowa colleges and universities.¹⁴²

While the state hotel and motel tax is now a special excise tax, it is nonetheless required to be administered, as nearly as possible, in the same manner as the sales tax.¹⁴³ State hotel and motel tax revenues are collected by the lessors of lodging, remitted to the Department of Revenue, and deposited in the General Fund of the State.¹⁴⁴

2. The Construction Equipment Tax¹⁴⁵

Like hotel and motel rentals, construction equipment sales were once taxed under the sales tax, but certain types of sales were removed from the sales tax base in order to maintain a uniform tax base for the sales and use taxes. Certain equipment sales

¹⁴⁰ See generally Iowa Code ch. 423A.

¹⁴¹ Iowa Code §§423A.2(1)(c), 423A.3.

¹⁴² Iowa Code §423A.5.

¹⁴³ Iowa Code §423A.6.

¹⁴⁴ Iowa Code §§423A.3, 423A.6.

¹⁴⁵ Iowa Code ch. 423D.



are now subject to a special excise tax and such sales are exempt from the sales and use tax.

The construction equipment tax is imposed at a rate of 5 percent on the sale or use of self-propelled building equipment, pile drivers, and motorized scaffolding, including replacement parts, and including auxiliary attachments that improve the equipment's performance, safety, operation, or efficiency, that are directly and primarily used by contractors in construction.¹⁴⁶ The tax does not apply if the equipment is leased or rented.¹⁴⁷

Also, like the state hotel and motel tax, the construction equipment tax is required to be administered, as nearly as possible, in the same manner as the sales tax.¹⁴⁸ Construction equipment tax revenues are collected by the retailer or user, remitted to the Department of Revenue, and deposited in the General Fund of the State.¹⁴⁹

3. The Real Estate Transfer Tax¹⁵⁰

The real estate transfer tax is imposed on sales of real estate in which the market value of the property exceeds \$500. The tax is imposed at the rate of 80 cents for each \$500 of value, or fraction thereof, in excess of \$500.¹⁵¹ Numerous exceptions to the tax are provided under Iowa law, including but not limited to deeds in which the consideration is \$500 or less, contracts for deed, transfers to or from the federal government, deeds for cemetery lots, corrective deeds, certain deeds between business entities and their owners or members during an incorporation or dissolution, deeds between former spouses under a decree of dissolution, and deeds transferring property to heirs at law or devisees under a will.¹⁵²

The tax is payable to the county recorder when the deed or other instrument conveying the real property is presented for recording, and such payment is noted on the instrument of transfer.¹⁵³ Sales involving parcels in more than one county require separate declarations of value to be filed with, and separate payment of tax to, each of the counties involved.¹⁵⁴

Real estate transfer tax revenues are divided between the county and the state. The county is allowed to retain 17.25 percent of the total revenues, and the remaining revenues are divided as follows: 65 percent are deposited in the General Fund of the State, 30 percent are deposited in the Housing Trust Fund (not to exceed \$3 million per fiscal year), and 5 percent are deposited in the Shelter Assistance Fund.¹⁵⁵ If the

¹⁴⁶ Iowa Code §§423D.1, 423D.2. "Contractor" includes contractors, subcontractors, and builders, but not owners. "Construction" means new construction, reconstruction, alterations, expansion, or remodeling of real property or structures.

¹⁴⁷ Iowa Code §423D.3.

¹⁴⁸ Iowa Code §423D.4.

¹⁴⁹ Iowa Code §§423D.2, 423D.4.

¹⁵⁰ Iowa Code ch. 428A.

¹⁵¹ Iowa Code §428A.1.

¹⁵² See Iowa Code §428A.2 for a full list of real estate transfer tax exceptions.

¹⁵³ Iowa Code §§428A.4, 428A.5.

¹⁵⁴ Iowa Code §428A.1.

¹⁵⁵ Iowa Code §428A.8.



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transfer to the Housing Trust Fund would exceed \$3 million in a fiscal year, the excess shall be deposited in the General Fund of the State.¹⁵⁶

4. Cigarette and Tobacco Taxes¹⁵⁷

In Iowa, cigarettes and other tobacco products are taxed separately. The cigarette tax is imposed at the rate of 6.8 cents per cigarette.¹⁵⁸ Since cigarettes are typically packaged and sold in packs of 20, the effective tax rate is \$1.36 per pack. However, the tax is 3.06 cents per cigarette (61.2 cents per pack) if such cigarette is dispensed from a cigarette vending machine into which loose tobacco products are inserted.¹⁵⁹ Little cigars are taxed at the same rate and in the same manner as cigarettes.¹⁶⁰

The tax is to be paid by the person making the “first sale” in the state, which means the first sale or distribution in this state or the first use or consumption in this state.¹⁶¹ Proof of tax payment is shown by a stamp affixed to, or imprinted on, each cigarette package.¹⁶² If the tax is not paid by the person making the “first sale,” the tax is imposed upon the person in possession, but does not apply to quantities of 40 cigarettes or less brought into this state for personal use.¹⁶³

Snuff is taxed separately at the rate of \$1.19 per ounce, or a proportion thereof for fractional amounts.¹⁶⁴ The tax on snuff is imposed on a distributor who imports snuff into the state, manufactures snuff in the state, or ships snuff to retailers in the state.¹⁶⁵ If the tax is not paid by the distributor, the tax is imposed at the same rate upon the consumer for the use and storage of the snuff in the state, but does not apply to quantities of less than 10 ounces.¹⁶⁶

Other tobacco products not referenced above are subject to the tobacco products tax at an effective rate of 50 percent of the wholesale price.¹⁶⁷ Despite this 50 percent rate, the tax on cigars cannot exceed 50 cents per cigar.¹⁶⁸ If the tax is not paid by the distributor, the tax is imposed at the same rate upon the consumer for the use and storage of the tobacco in the state, but does not apply to quantities of less than 25 cigars or less than one pound of other tobacco.¹⁶⁹

¹⁵⁶ Iowa Code §428A.8(3).

¹⁵⁷ Iowa Code ch. 453A.

¹⁵⁸ Iowa Code §453A.6.

¹⁵⁹ Iowa Code §453A.6(8). See Iowa Code §453A.1(5) for definition of “cigarette vending machine.”

¹⁶⁰ Iowa Code §§453A.42(5), 453A.43(1)(d).

¹⁶¹ Iowa Code §§453A.1(14), 453A.6(2). Taxes due on cigarettes dispensed from loose tobacco cigarette vending machines are required to be paid directly by the permit holder. Iowa Code §453A.6(8)(a).

¹⁶² Iowa Code §453A.6(3).

¹⁶³ Iowa Code §453A.6(2).

¹⁶⁴ Iowa Code §453A.43(3), (4).

¹⁶⁵ Iowa Code §453A.43(3)(a)-(c).

¹⁶⁶ Iowa Code §453A.43(4).

¹⁶⁷ Iowa Code §453A.43(1)(a), (b).

¹⁶⁸ Iowa Code §453A.43(1)(c).

¹⁶⁹ Iowa Code §453A.43(2).



Finally, in the event of a tobacco tax rate increase, the state imposes an inventory tax on the inventories of all tobacco products in an amount equal to the difference between the prior tax paid and the amount due after the tax rate increase.¹⁷⁰ Persons subject to the inventory tax are required to take inventory and report the tax due.¹⁷¹

Most revenues generated from the tobacco taxes are deposited in the Health Care Trust Fund.¹⁷²

5. Beer, Wine, and Liquor Taxes¹⁷³

Iowa used to be the exclusive seller in the state of alcohol, wine, and most beer. The state has largely relinquished its role as a distributor of wine and beer in favor of beer barrel and wine gallonage taxes. However, it still retains a monopoly on the wholesale distribution of liquor to retailers.¹⁷⁴

Under the barrel tax, beer is taxed at a rate of \$5.89 per barrel of 31 gallons, or a proportional amount for each fractional part of a barrel, sold at wholesale in Iowa.¹⁷⁵ Wine is taxed at the rate of \$1.75 per gallon, or a proportional amount for each fractional part of a gallon, sold at wholesale or through direct shipment in Iowa.¹⁷⁶ The barrel and wine gallonage taxes are collected from licensed wholesalers¹⁷⁷ who must also obtain the appropriate permits and pay the necessary fees in order to distribute beer and wine in the state.¹⁷⁸ Revenues from beer permit fees and the barrel tax are generally deposited in the General Fund of the State, but certain fees are allowed to be retained by local authorities or are deposited in the Beer and Liquor Control Fund, and barrel tax revenues collected on beer manufactured in Iowa from the owner and operator of a brewery are credited to the Barrel Tax Fund and used by the Economic Development Authority for the promotion of wine and beer made in Iowa.¹⁷⁹ Wine gallonage tax revenues from wine manufactured in, or shipped from, Iowa are deposited in the Wine Gallonage Tax Fund and distributed as follows: the first \$250,000 goes to the Midwest Grape and Wine Industry Institute at Iowa State University, then the remaining balance goes to the Iowa Economic Development Authority for the promotion of wine and beer made in Iowa.¹⁸⁰ Wine gallonage tax revenues from wine imported into Iowa are deposited in the Beer and Liquor Control Fund.¹⁸¹

¹⁷⁰ Iowa Code §453A.40.

¹⁷¹ Iowa Code §453A.40(2).

¹⁷² Iowa Code §§453A.35, 453A.35A.

¹⁷³ Iowa Code ch. 123.

¹⁷⁴ Iowa Code §§123.22, 123.24.

¹⁷⁵ Iowa Code §123.136.

¹⁷⁶ Iowa Code §§123.183, 123.187(4)(a).

¹⁷⁷ Iowa Code §§123.136, 123.183.

¹⁷⁸ Iowa Code §§123.125-123.127, 123.134, 123.173, 123.173A, 123.179. Permits, licenses, or fees are also required for or imposed upon other persons involved in the Iowa alcoholic beverage industry, but those are outside the purview of this Guide.

¹⁷⁹ Iowa Code §§123.143, 15E.117. See Iowa Code §123.53 for provisions related to the Beer and Liquor Control Fund.

¹⁸⁰ Iowa Code §§123.183, 15E.117.

¹⁸¹ Iowa Code §123.183(3).



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While there is, technically speaking, no tax imposed on liquor sales, the state, in its exclusive role as liquor wholesaler, sells liquor to retailers at a profit. This profit is referred to as the “markup” and may not exceed 50 percent of the wholesale price paid by the state.¹⁸² However, the markup of selected kinds of liquor may be increased above 50 percent if the average return on all sales of liquor does not exceed the wholesale price and the 50 percent markup.¹⁸³ Also, a bottle surcharge may be assessed to cover costs of providing for proper disposal of containers.¹⁸⁴

E. Motor Vehicle and Fuel-Related Taxes and Fees

Many motor vehicle taxes and fees can also be considered special excise taxes, but for convenience and because in Iowa the bulk of the revenues from motor vehicle and fuel-related taxes and fees is reserved for deposit in the Road Use Tax Fund, these taxes and fees are discussed separately in this Guide.¹⁸⁵

1. Fee for New Registration

The owners of motor vehicles subject to registration¹⁸⁶ are subject to a “fee for new registration” imposed on the purchase price of the vehicle at a rate of 5 percent.¹⁸⁷ Several deductions from the purchase price and exemptions from the fee are provided, including but not limited to dealer cash rebates, trade-in values, certain trades and transfers involving family members or related businesses and owners, vehicles purchased or sold by certain nonprofit organizations or government agencies, vehicles for which similar tax or registration fees have been paid in another state, certain vehicles purchased for subsequent rental, certain vehicles purchased by dealers and wholesalers for resale or for use by customers, and certain repossessed vehicles.¹⁸⁸

The 5 percent fee for new registration is also imposed on the lease of vehicles if the gross vehicle weight rating is less than 16,000 pounds and the vehicle is leased for 12 months or more.¹⁸⁹ Leases to certain nonprofit organizations or government

¹⁸² Iowa Code §123.24(4).

¹⁸³ Iowa Code §123.24(4).

¹⁸⁴ Iowa Code §123.24(5).

¹⁸⁵ For more information on the Road Use Tax Fund, see the Legislative Guide entitled Road Use Tax Fund, *available at* <https://www.legis.iowa.gov/publications/legalPubs/legisGuides> (last visited September 29, 2015).

¹⁸⁶ See, generally, Iowa Code ch. 321.

¹⁸⁷ Iowa Code §321.105A. Until somewhat recently, Iowa imposed a 5 percent use tax on the purchase price of motor vehicles subject to registration in Iowa. In 2008, the use tax was repealed in the “TIME-21” legislation and replaced with the “fee for new registration.” See 2008 Iowa Acts, ch. 1113 (SF 2420). In limited situations the sale of a motor vehicle is still subject to the sales and use tax. For more information, see Part VII, Section E of the Legislative Guide entitled State Taxation — Sales and Use Tax, *available at* <https://www.legis.iowa.gov/publications/legalPubs/legisGuides> (last visited September 29, 2015). Vehicles are also subject to other annual and one-time fees. For a description of those fees, see the Legislative Guide entitled Road Use Tax Fund, *available at* <https://www.legis.iowa.gov/publications/legalPubs/legisGuides> (last visited September 29, 2015).

¹⁸⁸ See Iowa Code §321.105A(2)(a)-(c).

¹⁸⁹ Iowa Code §321.105A(3). In limited situations the lease or rental of a motor vehicle is still subject to the sales and use tax. For more information, see Part VII, Section E of the Legislative Guide entitled State Taxation — Sales and Use Tax.



agencies are exempt.¹⁹⁰ The fee is computed on each separate lease transaction by multiplying the tax rate by the total lease payments, plus the down payment, and excluding title fees, annual registration fees, the fee for new registration, federal excise taxes, optional service or warrant contracts subject to the sales tax, insurance, manufacturer's rebate, refundable deposits, and finance charges.¹⁹¹

The fee for new registration is paid to the county treasurer by the owner of the vehicle or the lessee.¹⁹² County treasurers are responsible for remitting the fees to the Department of Revenue¹⁹³ which then deposits the moneys in the Road Use Tax Fund.¹⁹⁴ Refunds of the fee are allowed only in the case of vehicles returned for the full purchase price.¹⁹⁵

2. The Automobile Rental Excise Tax¹⁹⁶

Iowa imposes a 5 percent excise tax on the rental price of automobiles rented for a period of 60 days or less.¹⁹⁷ To be subject to the automobile rental excise tax, the rental must be subject to the sales and use tax, and the automobile must be subject to registration in any state, have a gross weight of 13 tons or less, and be designed primarily for carrying nine passengers or less.¹⁹⁸ The automobile rental excise tax is imposed in addition to the sales and use tax. Revenues collected from the automobile rental excise tax are deposited in the Statutory Allocations Fund to be used for various purposes.¹⁹⁹

3. Motor Fuel Taxes²⁰⁰

Iowa imposes an excise tax on most types of motor fuel sold in the state.²⁰¹ The tax is imposed on a per gallon basis and the rate differs based on the type of fuel:

¹⁹⁰ Iowa Code §321.105A(3)(f).

¹⁹¹ Iowa Code §321.105A(3)(b).

¹⁹² Iowa Code §§321.105A(2)(u1), 321.105A(3)(a).

¹⁹³ Iowa Code §§321.105A(2)(u1), 331.557.

¹⁹⁴ Iowa Code §321.145.

¹⁹⁵ Iowa Code §321.105A(6).

¹⁹⁶ Iowa Code ch. 423C.

¹⁹⁷ Iowa Code §423C.3. See also Iowa Code §423C.2(5) for definition of "rental."

¹⁹⁸ See Iowa Code §§423.2(6)(a), 423C.2(1), (5), 423C.3(1).

¹⁹⁹ Iowa Code §§423C.5, 321.145(2).

²⁰⁰ Iowa Code ch. 452A.

²⁰¹ Iowa Code §452A.3.



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Fuel Type	Tax Rate (Per Gallon)
Gasoline	<ul style="list-style-type: none"> • \$0.30 to \$0.31 (variable) until June 30, 2020²⁰² • \$0.30 after June 30, 2020²⁰³
Ethanol blended gasoline	<ul style="list-style-type: none"> • \$0.29 to \$0.30 (variable) until June 30, 2020²⁰⁴ • \$0.30 after June 30, 2020²⁰⁵
E-85 gasoline	<ul style="list-style-type: none"> • \$0.17 or the same rate as gasoline (variable)²⁰⁶
Biodiesel blended fuel	<ul style="list-style-type: none"> • \$0.295 to \$0.325 (variable) until June 30, 2020²⁰⁷ • \$0.325 after June 30, 2020²⁰⁸
Diesel fuel	\$0.325 ²⁰⁹
Aviation gasoline	\$0.08 ²¹⁰
Liquefied petroleum (used as special fuel)	\$0.30 ²¹¹
Compressed natural gas (used as special fuel)	\$0.31 ²¹²
Liquefied natural gas (used as special fuel)	\$0.325 ²¹³
Special fuel for aircraft	\$0.05 ²¹⁴
Other special fuels	same rate as gasoline ²¹⁵

Before July 1, 2020, the rates for gasoline, ethanol blended gasoline, E-85 gasoline, and biodiesel fuel will vary each year within the ranges described above based on actual fuel distributions in the state during the prior calendar year, as determined by the Department of Revenue.²¹⁶ The motor fuel excise taxes are generally collected from suppliers and then added into the selling price when the fuel is sold to consumers.²¹⁷ Revenues from the motor fuel excise taxes are deposited in

²⁰² Iowa Code §452A.3(1).

²⁰³ Iowa Code §452A.3(2).

²⁰⁴ Iowa Code §452A.3(1).

²⁰⁵ Iowa Code §452A.3(2).

²⁰⁶ Iowa Code §452A.3(3), (4).

²⁰⁷ Iowa Code §452A.3(6)(a)(2).

²⁰⁸ Iowa Code §452A.3(6)(a)(1), (2).

²⁰⁹ Iowa Code §452A.3(6)(a)(1), (2).

²¹⁰ Iowa Code §452A.3(5).

²¹¹ Iowa Code §452A.3(7).

²¹² Iowa Code §452A.3(8).

²¹³ Iowa Code §452A.3(9).

²¹⁴ Iowa Code §452A.3(6)(a)(3).

²¹⁵ Iowa Code §452A.3(6)(a)(4).

²¹⁶ Iowa Code §452A.3(1), (6).

²¹⁷ Iowa Code §452A.3(10), (11).



the Road Use Tax Fund.²¹⁸ However, taxes collected from the fuel used in watercraft and aircraft are deposited in the Marine Fuel Tax Fund and the Aviation Fuel Tax Fund, respectively, and used for special purposes.²¹⁹

A refund, or income tax credit in certain circumstances, is allowed for taxes paid for motor fuel or undyed (taxable) special fuels used by the federal government; the state and its agencies and political subdivisions; an Iowa urban transit system or a company that operates a taxicab service under contract with an Iowa urban transit system; a regional transit system; and a benefited fire district; for fuels used in unlicensed vehicles, stationary engines, and implements used in agricultural production and in machinery and equipment used for nonhighway purposes; for fuels used in producing denatured alcohol; for fuels used for idle time, power takeoffs, fuel lost through casualty, and blending errors for special fuel; fuels used by a bona fide commercial fisher; fuels used in the extraction and processing of natural deposits; undyed special fuel used in watercraft; and racing fuel.²²⁰

4. The Environmental Protection Charge²²¹

The environmental protection charge is a tax on the handling and storage of petroleum. When petroleum is handled and stored, some of it is inevitably “lost” in the process. The amount of the charge is based on the amount of this loss which is referred to as “diminution” and defined as “petroleum released into the environment prior to its intended beneficial use.”²²²

The amount of the charge is determined annually by the Iowa Comprehensive Petroleum Underground Storage Tank Board. The board determines the amount of the charge according to the following formula:

$$(\text{Volume}) \times (\text{Diminution Rate}) \times (\text{Cost Factor}) = \text{Charge}$$

“Volume” is the total amount of petroleum deposited in the tank. “Diminution rate” is set by statute at one-tenth of 1 percent. “Cost factor” is an amount per gallon set at least annually by the board. The “cost factor” must be \$10, or an amount reasonably calculated by the board to generate average annual revenue of \$17 million, whichever is greater.²²³ Typically, the cost factor has been the amount reasonably calculated to generate \$17 million.

The charge is administered and collected like an excise tax. Depositors of petroleum collect the charge from the owners and operators of storage tanks when the petroleum is deposited in the tank, and the depositor in turn remits the amount collected to the Department of Revenue which administers the tax.²²⁴ Revenues from the charge, like other motor-fuel-related taxes, are deposited in the Road Use Tax

²¹⁸ Iowa Const. art. VII, §8; Iowa Code §452A.79.

²¹⁹ Iowa Code §§328.56, 452A.79A, 452A.82, 452A.84.

²²⁰ Iowa Code §452A.17. See Iowa Code §§422.110, 422.111 for income tax credit in lieu of refund.

²²¹ Iowa Code ch. 424.

²²² Iowa Code §424.2(7).

²²³ Iowa Code §424.3.

²²⁴ Iowa Code §424.3(1).



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Fund.²²⁵ The environmental protection charge is set to be repealed effective June 30, 2016.²²⁶

F. Locally Imposed Taxes Administered by the State

In Iowa, there are several locally imposed taxes that are so closely related to certain state taxes that both the local and state taxes are administered together. In these instances, the taxes are typically imposed on the same tax base and collected together. The revenues from the locally imposed tax are accounted for by the state and distributed back to the local governments.

While closely related to their state-imposed counterparts, the locally imposed versions have a few distinguishing features. First, the Home Rule Amendments of the Iowa Constitution limit the taxing power of local governments by requiring that they be specifically authorized by the state to levy a tax.²²⁷ This gives the state a significant role in overseeing tax policy at the local level. Second, the legislation authorizing these taxes typically requires, or allows, some form of local electoral approval in order to be imposed, repealed, or changed. This requires close coordination between local governments and the state agencies administering the taxes.

1. Local Option Hotel and Motel Tax²²⁸

Cities and counties may impose a hotel and motel tax at the local level upon the motion of a city council or board of supervisors and after an election at which a majority of those voting favors imposition.²²⁹ When imposed by a city, only registered voters of the city are permitted to vote, and the tax only applies within the corporate boundaries of the city.²³⁰ When imposed by a county, only registered voters of the unincorporated areas are permitted to vote, and the tax only applies within the unincorporated areas of the county.²³¹ A majority vote is also required for a repeal or rate change, but a repeal or rate reduction is not allowed if there are outstanding bonds related to the tax, unless sufficient funds are set aside to pay the obligations.²³²

The local rate may not exceed 7 percent and must be in increments of one or more full percentage points.²³³ The tax applies to the same lodging rentals as those subject to the state-imposed hotel and motel tax discussed above in Part III, Section C, Subsection 1, of this Guide, except that lodging furnished for a religious retreat or function by a religious institution on land exempt from property tax is not subject to the tax.²³⁴ The local hotel and motel tax is collected by the lessors of lodging, remitted to

²²⁵ Iowa Code §424.7(4).

²²⁶ Iowa Code §424.19.

²²⁷ Iowa Const. art. III, §§38A (municipalities), 39A (counties).

²²⁸ Iowa Code §423A.4.

²²⁹ Iowa Code §423A.4(4). The Iowa Department of Revenue maintains a list of all jurisdictions imposing the local hotel and motel tax, available at <https://tax.iowa.gov/report/Hotel-Motel?combine=Jurisdiction> (last visited October 14, 2015).

²³⁰ Iowa Code §§423A.4(1), 423A.4(4)(b).

²³¹ Iowa Code §§423A.4(1), 423A.4(4)(b).

²³² Iowa Code §423A.4(4).

²³³ Iowa Code §423A.4(1).

²³⁴ Iowa Code §423A.5(2)(b).



the Department of Revenue, and deposited in the Local Transient Guest Tax Fund to be distributed back to the appropriate cities and counties.²³⁵ These counties and cities are required to use at least 50 percent of their hotel and motel tax revenues for recreation, convention, cultural, or entertainment facilities or for the promotion and encouragement of tourist and convention business in the city or county and surrounding areas.²³⁶

2. Local Option Sales Tax and Vehicle Tax²³⁷

a. In General. Counties may impose a sales tax and a vehicle tax at the local level upon a petition of the voters or motions of city councils or the board of supervisors and after an election at which a majority of those voting favors imposition.²³⁸ The two taxes may be imposed separately or together. When imposed, the sales tax only applies to those incorporated areas and the unincorporated area in which a majority of those voting in the area favored imposition, while the vehicle tax applies to the entire county.²³⁹ For purposes of the sales tax vote, cities contiguous to each other are treated as one incorporated area. A majority vote is also required for a repeal or rate change, or the governing body on its own motion may repeal the sales tax, but a repeal or rate reduction of the sales tax is not allowed if there are outstanding bonds related to the tax, unless sufficient funds are set aside to pay the obligations.²⁴⁰

b. Local Option Sales Tax. The local option sales tax rate may not exceed 1 percent, and applies to the same sales and services as are subject to the state sales tax, with a few exceptions.²⁴¹ The tax is not imposed on motor fuel or special fuel consumed for highway use or in watercraft or aircraft if the fuel tax is paid and a refund has not or will not be allowed, or on sales of equipment by the Iowa Department of Transportation.²⁴²

If the local option sales tax is imposed, a local excise tax is also imposed on the purchase price of natural gas, natural gas service, electricity, and electric service that is subject to the state use tax and used within the area where the local sales tax is

²³⁵ Iowa Code §§423A.6, 423A.7.

²³⁶ Iowa Code §423A.7(4)(a). Examples of appropriate facilities include but are not limited to memorial buildings, halls and monuments, civic center convention buildings, auditoriums, coliseums, and related parking areas.

²³⁷ See generally Iowa Code ch. 423B. There is no corresponding local option use tax.

²³⁸ Iowa Code §423B.1(1), (3), (4). Voter petitions must be signed by eligible voters in the county equal in number to 5 percent of those who voted in the last general election. When city councils or the board of supervisors adopts a motion, those governing bodies must represent a threshold of at least 50 percent of the population of the county. The Iowa Department of Revenue maintains a list of all jurisdictions imposing local sales taxes, *available at* <https://tax.iowa.gov/iowa-local-option-tax-information> (last visited October 14, 2015).

²³⁹ Iowa Code §§423B.1(3), 423B.1(6)(a).

²⁴⁰ Iowa Code §§423B.1(6)(a)(2), 423B.1(9), (10), 423B.9. An automatic repeal may be provided for on the ballot for imposition of the sales tax. Iowa Code §423B.1(6)(a)(3).

²⁴¹ Iowa Code §423B.5. For a detailed discussion of the Iowa sales and use tax, see the Legislative Guide entitled State Taxation — Sales and Use Taxes, *available at* <https://www.legis.iowa.gov/publications/legalPubs/legisGuides> (last visited September 25, 2015).

²⁴² Iowa Code §423B.5(u1).



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imposed.²⁴³ However, these utilities are exempt if the sale or use is subject to a franchise fee or user fee.²⁴⁴

The local option sales tax only applies to sales occurring, and services performed, within the area imposing the tax (taxing area).²⁴⁵ This generally includes sales of goods for which delivery is made within the taxing area, i.e., physical possession of the goods are transferred to the buyer.²⁴⁶ However, when goods are transferred into or out of the taxing area via common carrier, the sale is usually deemed to occur where physical possession of the goods is transferred to the common carrier, unless the terms of delivery between buyer and seller indicate that title and risk of loss pass at a different location.²⁴⁷ If a service is performed inside and outside a taxing area, it is presumed that the entire service is performed within the taxing area unless that portion of the service performed outside the taxing area is separately stated, separately billed, and reasonable in amount.²⁴⁸

The local option sales tax is collected by retailers in conjunction with the state sales tax, and both taxes are remitted to the Department of Revenue, which then accounts for and distributes the local option sales tax revenues back to the local governments according to a statutory formula involving population and property tax revenues.²⁴⁹

c. Local Option Vehicle Tax. The local vehicle tax applies to all vehicles subject to the state-imposed annual registration requirement and that are registered to residents of the county imposing the tax. The tax may only be imposed on renewals of registrations. The tax is imposed per vehicle at a rate specified on the ballot proposition approving the imposition of the tax.²⁵⁰

The local option vehicle tax is collected by county treasurers with the assistance of the Department of Transportation, and the revenues are divided among city and county governments based on the vehicle owner's residence. The revenues are required to be used solely for public transit or shall be credited to the street construction fund of the city or the secondary road fund of the county.²⁵¹

3. Local Income Surtaxes

a. In General. Local governments may impose school district income surtaxes and an emergency medical services income surtax. These surtaxes are imposed on individuals residing within the school district or county, respectively, as a percentage of

²⁴³ Iowa Code §423B.5.

²⁴⁴ Iowa Code §423B.5.

²⁴⁵ See generally Iowa Admin. Code 701-107.3 through 701-107.5.

²⁴⁶ Iowa Admin. Code 701-107.3(1).

²⁴⁷ Iowa Admin. Code 701-107.3(2).

²⁴⁸ Iowa Admin. Code 701-107.5(1).

²⁴⁹ Iowa Code §§423B.6, 423B.7.

²⁵⁰ Iowa Code §§423B.2, 321.40, 321.105.

²⁵¹ Iowa Code §423B.3.



the individual's income tax liability, and are collected with the individual income tax return.²⁵² The cumulative surtax rate for a school district for all income surtaxes may not exceed 20 percent of any individual's state income tax liability.²⁵³ Taxpayers report their local income surtaxes on their state income tax returns.

b. School District Income Surtax. Boards of school districts may call an election or may on their own motion (subject to petition for election from the voters) impose, in conjunction with a property tax levy, an income surtax for additional funding for the school district under the instructional support program,²⁵⁴ the educational improvement program,²⁵⁵ and the physical plant and equipment levy.²⁵⁶ All revenue collected from a surtax is remitted to the local school district imposing the surtax, except for the portion remitted to the Department of Revenue to cover costs incurred in administering the surtax.

c. Emergency Medical Services Income Surtax. The emergency medical services income surtax was enacted in 1992. A county board of supervisors may offer for voter approval a local option income surtax, a property tax, or a combination of the two taxes to generate revenues for emergency medical services. The income surtax may be imposed for a maximum period of five years. All revenue collected from the surtax is remitted to the county imposing the surtax, except for the portion remitted to the Department of Revenue to cover costs incurred in administering the surtax.²⁵⁷ The surtax was imposed for the first time in the 1995 tax year by Appanoose County. As of 2015, no other county is imposing the surtax.

G. Inheritance Taxes²⁵⁸

When a person dies, the person's property is passed to others in a variety of different ways. The inheritance tax is a charge for transferring that property from the decedent owner to the beneficiaries, and each beneficiary is potentially responsible for paying tax on the amount inherited.

A decedent's property, referred to as the estate, may include real estate and tangible personal property located in the state (regardless of whether the decedent was a resident), and intangible personal property if the decedent was domiciled in the state.²⁵⁹ The inheritance tax is imposed on the net market value of property passing from the decedent's

²⁵² Iowa Code §§257.21, 257.29, 298.2, 422D.2. For purposes of the local government income surtaxes, state tax liability is equal to the individual's income tax less all nonrefundable income tax credits except the Iowa Taxpayers Trust Fund tax credit. In light of the U.S. Supreme Court's ruling in *Comptroller of Treasury of Maryland v. Wynne*, 135 S.Ct. 1787 (2015), the Department of Revenue will allow the out-of-state tax credit to be claimed against the local government surtaxes. Prior to that ruling, it was the Department's practice to calculate the surtax prior to applying the out-of-state tax credit. See <https://tax.iowa.gov/wynne-decision> (last visited October 29, 2015). For a detailed discussion of the Iowa Individual Income Tax, including the out-of-state tax credit, see the Legislative Guide entitled State Taxation: Iowa Individual Income Tax, available at <https://www.legis.iowa.gov/publications/legalPubs/legisGuides>.

²⁵³ Iowa Code §298.14.

²⁵⁴ Iowa Code §§257.18, 257.27.

²⁵⁵ Iowa Code §257.29.

²⁵⁶ Iowa Code §298.2.

²⁵⁷ Iowa Code ch. 422D.

²⁵⁸ Iowa Code ch. 450, 450B.

²⁵⁹ Iowa Code §450.2.



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estate to beneficiaries by virtually any method, including by will, by Iowa's intestacy laws, through ownership by joint tenancy, and even by certain gifts made prior to a decedent's death.²⁶⁰

In the context of the inheritance tax, "net market value" refers to the fair market value of the total estate at the time of the decedent's death, less allowable deductions relating to outstanding debts, state and local taxes accrued before death, federal taxes owed at death, reasonable funeral expenses, court-ordered allowance for support of the surviving spouse and minor children, court costs, and certain other administrative expenses.²⁶¹ However, two other valuations may be used if a similar election is made for federal estate tax purposes. Both of these valuations are determined according to provisions of the Internal Revenue Code. First, the estate may, at the election of the personal representative, choose an alternate valuation which values the estate property as of the date six months after the decedent's death.²⁶² Second, certain qualified heirs who are transferred real property used by the decedent in farming or another closely held business may elect a reduced "qualified use valuation" on that qualified real property.²⁶³ It should be noted that if within 10 years and before the death of the qualified heir, the qualified real property is disposed of or ceases to be used for the qualified use, an additional qualified use inheritance tax is due equal to the difference between the amount of inheritance tax paid and the amount of inheritance tax that would have been due had the qualified use valuation not been elected.²⁶⁴

Since the inheritance tax is imposed on the transfer of a decedent's property, the requirement to pay the tax falls on the person who becomes beneficially entitled to the property.²⁶⁵ However, there are a number of significant exemptions provided that limit the amount of tax due and the number of beneficiaries who owe it.²⁶⁶ Most significantly, a decedent's surviving spouse, lineal ascendants (parents, grandparents, etc.), lineal descendants (adopted or biological children, grandchildren, etc.), and stepchildren and their lineal descendants (adopted or biological), are not required to pay the tax.²⁶⁷ The tax is not collected on estates valued at \$25,000 or less, on property that passes to tax-exempt organizations for charitable, educational, or religious purposes, or on property that passes to Iowa hospitals, municipal corporations, public libraries, or public art galleries for purely public purposes.²⁶⁸ The tax is also not collected in a few other instances involving property in certain insurance proceeds, qualified Internal Revenue Code §529 (tuition) and §529A

²⁶⁰ Iowa Code §§450.2, 450.3.

²⁶¹ Iowa Code §450.12.

²⁶² Iowa Code §450.37(1)(b); IRC §2032.

²⁶³ Iowa Code §450B.2; IRC §2032A. A qualified heir is the spouse of a decedent, an ancestor of the decedent, a lineal descendant of the decedent, a lineal descendant of the decedent's parent, or the spouse of any such lineal descendant. Iowa Code §450B.1(2); IRC §2032A(e).

²⁶⁴ Iowa Code §§450B.3, 450B.5.

²⁶⁵ Iowa Code §450.5. It should be noted that it is the duty of a personal representative administering the estate to ensure that the inheritance tax is collected and paid, and a personal representative can be held jointly liable for the tax upon the failure to do so.

²⁶⁶ Iowa Code §§450.4, 450.9.

²⁶⁷ Iowa Code §450.9.

²⁶⁸ Iowa Code §450.4.



(disabled beneficiary) plans, qualified retirement accounts, on bequests for burial plots and up to \$500 for religious services, and on in-kind distributions of tangible personal property valued at \$5,000 or less.²⁶⁹

Inheritance tax rates range from 5 percent to 15 percent depending upon the amount of the inheritance and the relationship of the recipient to the decedent. Inheritance taxes for shares passing to a brother, sister, son-in-law, or daughter-in-law are taxed in six brackets, starting at 5 percent on the first \$12,500, up to 10 percent on all amounts over \$150,000. Shares passing to any other individual are taxed in three brackets, starting at 10 percent on the first \$50,000, up to 15 percent on all amounts over \$100,000. Shares passing for charitable, educational, or religious purposes to organizations that do not qualify as tax-exempt under the Internal Revenue Code are taxed at a rate of 10 percent. Shares passing in any other manner to for-profit organizations are taxed at a rate of 15 percent.²⁷⁰ Inheritance tax revenues are collected by the Department of Revenue and deposited in the General Fund of the State.²⁷¹

H. Racing and Gaming Taxes

Iowa imposes several taxes on gambling in the state. For an in-depth discussion of these taxes, and of gambling in Iowa, please see the Legislative Guide entitled *Gambling — Casinos and Racetracks*, available at <https://www.legis.iowa.gov/publications/legalPubs/legisGuides> (last visited October 20, 2015).

1. The Tax on Pari-Mutuel Wagering²⁷²

Iowa imposes a tax on pari-mutuel wagering, which is a form of wagering in which all bets are “pooled” together. Unlike fixed-odds wagering, in pari-mutuel wagering the final payout amount is not known until the pool is closed. Pari-mutuel wagering is allowed in Iowa on licensed horse and dog races.

The tax is imposed at the rate of 6 percent of the gross sum wagered at each horse race meeting, but certain credits are allowed to be used for debt retirement or operating expenses.²⁷³ The rate imposed on dog racing is either 4, 5, or 6 percent of the gross sum wagered during the dog race season, depending on how much is wagered during that season.²⁷⁴ There is a separate tax imposed at the rate of 2 percent of the gross sum wagered on horse and dog races that are simultaneously telecast.²⁷⁵ The tax is in lieu of the taxes otherwise imposed on horse or dog races. In addition, Iowa charges a license fee of \$200 per racing day for horse and dog racing, and a regulatory fee set by the state Racing and Gaming Commission for costs related to special agents and support costs for the Division of Criminal Investigations activities.²⁷⁶

²⁶⁹ Iowa Code §450.4.

²⁷⁰ Iowa Code §450.10.

²⁷¹ Iowa Code §§450.3, 450.6.

²⁷² Iowa Code ch. 99D.

²⁷³ Iowa Code §99D.15(1).

²⁷⁴ Iowa Code §99D.15(3).

²⁷⁵ Iowa Code §99D.15(4).

²⁷⁶ Iowa Code §99D.14(2), (3).



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The state Racing and Gaming Commission collects the tax on pari-mutuel wagering. The tax must be paid within 10 days after the close of a track's racing season.²⁷⁷ Revenues from the tax are shared with cities and counties according to a statutory formula.²⁷⁸ The state share of the taxes and fees are distributed among various funds in the state treasury.²⁷⁹

2. The Tax on Gambling Games²⁸⁰

Iowa imposes a tax on gambling games operated at racetracks, "land-based gambling structures" (i.e., casinos), and excursion boats.²⁸¹ The tax is imposed at the rate of 5 percent on the first \$1 million of adjusted gross receipts and 10 percent on the next \$2 million of adjusted gross receipts.²⁸² The rate imposed on adjusted gross receipts in excess of \$3 million varies:²⁸³

- For an excursion boat or casino, the rate is 22 percent.²⁸⁴
- For a racetrack located in a county with no excursion boat or casino, the rate is 24 percent.²⁸⁵
- For a racetrack located in a county where there is an excursion boat or casino, the rate is 22 percent if the racetrack has not been issued a table games license during the fiscal year or if the racetrack's adjusted gross receipts were less than \$100 million in the prior fiscal year.²⁸⁶
- For a racetrack located in a county where there is an excursion boat or casino, and the racetrack has been issued a table games license during the fiscal year (or prior fiscal year) and had adjusted gross receipts of \$100 million or more in the prior fiscal year, the rate is 22 percent on adjusted gross

²⁷⁷ Iowa Code §99D.15(1).

²⁷⁸ Iowa Code §99D.15.

²⁷⁹ Iowa Code §§8.57(5), 99D.17.

²⁸⁰ Iowa Code ch. 99F.

²⁸¹ Iowa Code §§99F.1, 99F.3, 99F.11.

²⁸² Iowa Code §99F.11(1).

²⁸³ The wagering tax has not been without controversy. At one time, gambling games were allowed on excursion boats but not at racetracks (or at land-based gambling structures such as casinos). In 1994, the Iowa General Assembly allowed gambling games to be conducted at racetracks but taxed them at rates as high as 36 percent while setting the top rate on excursion boats at just 20 percent. The racetracks filed suit challenging the higher tax rates. The Iowa Supreme Court held that the higher rate on racetracks violated the equal protection provisions of both the United States and Iowa constitutions. See *Racing Assoc. of Central Iowa v. Fitzgerald*, 648 N.W. 2d 555 (Iowa 2002). The federal aspects of that decision were reversed by the United States Supreme Court, which held that the different tax rates did not offend federal equal protection guarantees, and the case was remanded to the Iowa Supreme Court. See *Fitzgerald v. Racing Assoc. of Central Iowa*, 539 U.S. 103 (2003). On remand, the Iowa Supreme Court once again struck down the differential rates, this time under only the Iowa constitution's equal protection provision. See *Racing Assoc. of Central Iowa v. Fitzgerald*, 675 N.W. 2d 1 (2004). Subsequent to this litigation, the Iowa General Assembly adopted the current rate structure and authorized gambling games to be conducted at casinos in addition to racetracks and excursion boats. For more information on the scope of the federal Equal Protection Clause, see Part II of this Guide.

²⁸⁴ Iowa Code §99F.11(2)(a).

²⁸⁵ Iowa Code §99F.11(2)(c).

²⁸⁶ Iowa Code §99F.11(2)(b)(1).



receipts received prior to the operation of table games and 24 percent on adjusted gross receipts received on or after the operation of table games.²⁸⁷

Iowa also imposes certain fees on operators of gambling games.²⁸⁸ First, there is a fee charged in order to obtain a license. The fee is \$5 million for a licensee locating in a county with a population of 15,000 or less, \$10 million for locating in a county with a population of 15,000 to 100,000, and \$20 million for locating in a county with a population of 100,000 or more.²⁸⁹ One-fifth of the fee is payable upon the filing of the application for the license, and the remaining four-fifths is payable ratably over the next four years.²⁹⁰ For racetracks authorized to conduct table games, there is imposed an additional one-time table games licensing fee of \$3 million if its gambling game receipts in the previous fiscal year were less than \$100 million, or \$10 million if its gambling game receipts in the previous fiscal year were \$100 million or more.²⁹¹ But this additional licensing fee can be offset over five years by wagering taxes paid by the racetrack.²⁹² Second, excursion boats and casinos are charged an annual license fee of \$5 per person capacity, and racetracks are charged an annual license fee of \$1,000.²⁹³ Finally, nonracetrack licensees are required to pay regulatory fees related to special agents and support costs for the Division of Criminal Investigations activities.²⁹⁴

The tax on gambling games is collected by the State Treasurer and must be paid within 10 days after the close of the day when the wagers were made.²⁹⁵ Tax revenues are shared with cities and counties, and the state share is distributed among various funds in the state treasury.²⁹⁶

3. Monitor Vending Machines²⁹⁷

Legislation enacted in 2006 prohibited the Iowa Lottery Authority from allowing retailers to offer monitor vending machines (TouchPlay machines) to the public. The legislation, including the prohibition on machines, took effect March 20, 2006, but retailers who acquired a monitor vending machine prior to that date could continue to offer the machine to the public through May 3, 2006. On or after May 4, 2006, monitor vending machines are no longer permitted. If revenues are derived from monitor vending machines on or after May 4, 2006, an excise tax at the rate of 65 percent is imposed on any net monitor vending machine revenue receipts generated.²⁹⁸

²⁸⁷ Iowa Code §99F.11(2)(b)(2).

²⁸⁸ Cities and counties may adopt admission fees for embarking on excursion gambling boats. See Iowa Code §99F.10(3).

²⁸⁹ Iowa Code §99F.10(7).

²⁹⁰ Iowa Code §99F.10(7).

²⁹¹ Iowa Code §99F.4A(8).

²⁹² Iowa Code §99F.4A(8).

²⁹³ Iowa Code §§99F.4A(5), 99F.5(2).

²⁹⁴ Iowa Code §99F.10(4).

²⁹⁵ Iowa Code §99F.11(3).

²⁹⁶ Iowa Code §§8.57(5), 99F.11.

²⁹⁷ Iowa Code §99G.30A.

²⁹⁸ 2006 Iowa Acts, ch. 1005; Iowa Code §§99G.3(7), (9), 99G.30A.



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I. Other Taxes

There are some state taxes in Iowa that are not easily categorized according to the groupings used above. These taxes can be significant sources of revenue (unemployment compensation tax) or rather insignificant (drug stamp tax, brucellosis and tuberculosis eradication levy).

1. The Unemployment Compensation Tax²⁹⁹

a. In General. The unemployment compensation tax is imposed on the taxable wage base³⁰⁰ of most employers in order to finance Iowa's unemployment compensation program. The U.S. Department of Labor oversees the unemployment system, but each state administers and finances its own program. The Department of Workforce Development administers the program in Iowa. Revenues from the tax, referred to as "employer contributions," are held in the Unemployment Compensation Fund and the Unemployment Compensation Reserve Fund and used to pay benefits to eligible workers.³⁰¹ For a detailed discussion of unemployment compensation in Iowa, see the Legislative Guide entitled Unemployment Compensation Benefits in Iowa, available at <https://www.legis.iowa.gov/publications/legalPubs/legisGuides> (last visited October 20, 2015).

b. Entities Subject to Tax. Employers subject to the tax include: An employer that has one or more employees performing covered services for a portion of a day in at least 20 different calendar weeks or whose payroll in any calendar quarter is \$1,500 or more; an employer of agricultural laborers paying cash wages of \$20,000 or more in a calendar quarter or employing 10 or more workers in 20 separate weeks; and an employer of domestic help paying cash wages of \$1,000 or more during a calendar quarter. An Indian tribe is considered an employer in the same manner and under the same terms as a governmental entity.³⁰² Governmental entities, Indian tribes, and nonprofit organizations may elect to reimburse the Unemployment Compensation Fund for benefits paid rather than make contributions under the tax tables.³⁰³

c. Contribution Determination. Iowa uses a flexible method to determine the rate of employer contributions to the funds. This method incorporates a statutory

²⁹⁹ See generally Iowa Code ch. 96.

³⁰⁰ The "taxable wage base" is either two-thirds of the statewide average yearly wage or the taxable wage base for the federal unemployment tax, whichever is greater. Iowa Code §96.19(37) (definition of "taxable wages"). The taxable wage bases for 2015 and 2016 are \$27,300 and \$28,300, respectively. Employers pay unemployment compensation tax on each employee's wages up to the taxable wage base. See the Department of Workforce Development's Unemployment Insurance Handbook, pg. 13, available at https://www.iowaworkforcedevelopment.gov/sites/search.iowaworkforcedevelopment.gov/files/70-5007%20Handbook%20For%20Employers_0.pdf (last visited October 20, 2015).

³⁰¹ Iowa Code §96.9. The Unemployment Compensation Reserve Fund is used to pay benefits when moneys in the Unemployment Compensation Fund are insufficient. Iowa Code §96.9(8)(c). Each year the Unemployment Compensation Reserve Fund balance drops below \$150 million, a certain percentage of employer contributions collected are deemed to be reserve contributions and used to replenish the reserve fund. Iowa Code §96.9(8)(b). The director of the Department of Workforce Development determines the percentage, which is limited to not more than 50 percent of the contribution rate or \$50 million per calendar year. However, employers who are assigned a contribution rate of 5.4 percent do not have any contributions deposited in the reserve fund.

³⁰² Iowa Code §§96.19(16), 96.7(9).

³⁰³ Iowa Code §96.7(7)-(9).



mechanism for annually setting the amount of the tax on employers at a rate sufficient to meet the fund's needs for the year.

Each year by September 5, the Department of Workforce Development determines the contribution rate table to be used for the following year.³⁰⁴ This determination is made by (1) dividing the current reserve fund ratio³⁰⁵ by the highest benefit cost ratio³⁰⁶ and then (2) using that value to find the associated statutory contribution rate table that will be effective for the following year, as follows:³⁰⁷

Equals or exceeds	But is less than	The contribution rate table in effect shall be
—	0.3	1
0.3	0.5	2
0.5	0.7	3
0.7	0.85	4
0.85	1.0	5
1.0	1.15	6
1.15	1.30	7
1.30	—	8

In order to determine the appropriate tax rate from the table to be applied to a particular employer, each employer is given a rank based upon the employer's benefit ratio, which is determined by dividing the employer's five-year average unemployment benefit charges by the employer's five-year average taxable payroll amount.³⁰⁸ This ratio is then compared to all other employers to establish the employer's rank, with the lowest benefit ratio being ranked 1. Nonconstruction new employers are given the rank of 12 and pay a rate of not less than 1 percent for the first year.³⁰⁹ New construction employers are given the rank of 21 for the first year.³¹⁰

³⁰⁴ Iowa Code §96.7(2)(d).

³⁰⁵ The current reserve fund ratio is determined by adding \$150 million to the amount currently in the reserve fund and dividing that amount by the total wages paid in covered employment during the first four calendar quarters of the previous five calendar quarters. Iowa Code §96.7(2)(d)(1).

³⁰⁶ The benefit cost ratio for each year is the total benefits paid for the year divided by the total wages paid during that year. The highest benefit cost ratio is the highest of the benefit ratios for each of the previous 10 years. However, the highest benefit cost ratio cannot be less than .02. Iowa Code §96.7(2)(d)(2).

³⁰⁷ Iowa Code §96.7(2)(d)(2).

³⁰⁸ Iowa Code §96.7(2)(d)(2).

³⁰⁹ Iowa Code §96.7(2)(c)(1).

³¹⁰ Iowa Code §96.7(2)(c)(2).



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Employers use the effective contribution rate table and their employer rank to determine their tax rate according to the following table:³¹¹

Benefit Ratio Rank	Approximate Cumulative Taxable Payroll Limit	Contribution Rate Tables							
		1	2	3	4	5	6	7	8
1	4.8%	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
2	9.5%	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
3	14.3%	0.1	0.1	0.1	0.1	0.1	0.0	0.0	0.0
4	19.0%	0.4	0.3	0.3	0.2	0.1	0.1	0.1	0.1
5	23.8%	0.6	0.5	0.4	0.3	0.3	0.2	0.1	0.1
6	28.6%	0.9	0.8	0.6	0.5	0.4	0.3	0.2	0.1
7	33.3%	1.2	1.0	0.8	0.6	0.5	0.4	0.3	0.2
8	38.1%	1.5	1.3	1.0	0.8	0.6	0.5	0.3	0.2
9	42.8%	1.9	1.5	1.2	0.9	0.7	0.6	0.4	0.3
10	47.6%	2.1	1.8	1.4	1.1	0.8	0.6	0.5	0.3
11	52.4%	2.5	2.0	1.6	1.3	1.0	0.7	0.5	0.3
12	57.1%	3.0	2.4	1.9	1.5	1.1	0.9	0.6	0.4
13	61.9%	3.6	2.9	2.4	1.8	1.4	1.1	0.8	0.5
14	66.6%	4.4	3.6	2.9	2.2	1.7	1.3	1.0	0.6
15	71.4%	5.3	4.3	3.5	2.7	2.0	1.6	1.1	0.7
16	76.2%	6.3	5.2	4.1	3.2	2.4	1.9	1.4	0.9
17	80.9%	7.0	6.4	5.2	4.0	3.0	2.3	1.7	1.1
18	85.7%	7.5	7.5	7.0	5.4	4.1	3.1	2.3	1.5
19	90.4%	8.0	8.0	8.0	7.3	5.6	4.2	3.1	2.0
20	95.2%	8.5	8.5	8.5	8.0	7.6	5.8	4.3	2.8
21	100.0%	9.0	9.0	9.0	9.0	8.5	8.0	7.5	7.0

d. Sale or transfer by employer. When a sale or transfer of an organization, trade, or business occurs, a redetermination of the employer's contribution rate is generally required.³¹² The acquiring employer may assume the accounts and contribution rate of the previous employer if certain conditions are met, but the Department of Workforce Development has the authority to investigate and disallow the transfer, and instead tax the employer as a new employer, if it determines that the organization, trade, or business was acquired solely or primarily for the purpose of obtaining a lower contribution rate.³¹³ The department makes the determination based on objective factors that may include an evaluation of the sales price, the continuation of the business activity, and whether "a substantial number" of new employees were hired to perform duties unrelated to the business operated prior to the acquisition.³¹⁴ The department is required to assign an additional penalty contribution rate of 2

³¹¹ Iowa Code §96.7(2)(d)(2).

³¹² Iowa Code §96.7(2)(b).

³¹³ Iowa Code §96.7(2)(b)(3).

³¹⁴ Iowa Code §96.7(2)(b)(3).



percent of taxable wages and to assess civil penalties against a person who violates the provisions relating to the sale or transfer of an organization, trade, or business if such sale or transfer was made in order to receive a reduced contribution rate.³¹⁵ Such a violation constitutes an aggravated misdemeanor.³¹⁶ Civil penalties collected are deposited in the Unemployment Trust Fund and used for the payment of unemployment benefits.³¹⁷

2. The Tax on Dealers of Controlled Substances (The “Drug Stamp” Tax)³¹⁸

Iowa imposes a tax on dealers³¹⁹ of illegal substances, including controlled substances, counterfeit substances, simulated controlled substances, marijuana, or a mixture of materials that contain those substances.³²⁰ The tax is imposed at different rates depending on the substance, as follows:³²¹

- \$5 per gram or portion of a gram of processed marijuana.
- \$250 per gram or portion of a gram of a taxable substance, other than marijuana, that is sold by weight.
- \$750 per unprocessed marijuana plant.
- \$400 for each 10 dosage units or portion of 10 dosage units of a taxable substance, other than unprocessed marijuana plants, that is sold by weight.

A dealer of a taxable substance is prohibited from possessing, distributing, or offering the substance for sale unless the tax has first been paid and a stamp has been permanently affixed to the substance.³²² The tax is due and payable immediately upon the manufacture, production, acquisition, purchase, or possession of the taxable substance by the dealer.³²³ A stamp, label, or other official indicia that the tax has been paid must be purchased from the Department of Revenue. The minimum purchase of stamps is \$215.³²⁴ A dealer is entitled to a credit if taxes on the substance have already been paid to another state or local government.³²⁵ Revenues collected are deposited in the General Fund of the State.³²⁶

Failure to pay the tax and permanently affix the appropriate stamps subjects the dealer to a civil penalty equal to the amount of the taxes owed, as well as interest on both the taxes owed and the penalty.³²⁷ In addition, a failure to affix the stamp, the

³¹⁵ Iowa Code §96.16(5).

³¹⁶ Iowa Code §96.16(5).

³¹⁷ Iowa Code §96.16(5).

³¹⁸ Iowa Code ch. 453B.

³¹⁹ See Iowa Code §453B.1(3) for the definition of “dealer.”

³²⁰ Iowa Code §453B.1(10) (definition of “taxable substance”).

³²¹ Iowa Code §453B.7.

³²² Iowa Code §453B.3.

³²³ Iowa Code §453B.3.

³²⁴ Iowa Code §453B.8.

³²⁵ Iowa Code §453B.13.

³²⁶ Iowa Code §453B.2.

³²⁷ Iowa Code §453B.12.



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use of an expired or previously used tax stamp, or the creation, possession, or use of a counterfeit tax stamp are all class “D” felonies under Iowa law.³²⁸ The Director of Revenue may request and receive information about dealers of taxable substances from state and local officials and employees.³²⁹ However, the Director of Revenue may not reveal information obtained pursuant to the administration of the tax, and such information may not be used against the dealer in a criminal proceeding except proceedings under Iowa Code chapter 453B.³³⁰

3. The Brucellosis and Tuberculosis Eradication Levy³³¹

Iowa law requires the Secretary of Agriculture to manage a fund dedicated to the eradication of bovine brucellosis and tuberculosis. Each year on January 20, the secretary must determine whether the balance in the fund is sufficient to carry on the work of eradicating those diseases. If the balance is not sufficient, the secretary must notify the board of supervisors of each county to levy a property tax in an amount sufficient to meet the Department of Agriculture and Land Stewardship’s expenses.

The maximum amount of the levy is 33 and 3/4 cents per \$1,000 of assessed value of all taxable property in the county. County treasurers collect the tax and transmit the revenues to the treasurer of state who deposits them in the Brucellosis and Tuberculosis Eradication Fund.

IV. Tax Revenues

This part contains information on the amount of revenues collected under most of the taxes discussed in this Guide. The numbers reported here do not reflect the entirety of the state budget since there are significant nontax sources of revenue such as federal loans, grants and appropriations, state-imposed fees, and revenues from the operation of the State Lottery. This information is helpful in understanding the tax revenue mix but does not reflect revenue commitments. Some of the revenues reported are credited to special funds, such as motor fuel taxes to the Road Use Tax Fund, rather than to the General Fund of the State.

The numbers reported also do not include the gross amount of revenues collected. Instead, the numbers reflect the “net revenues” of the various state taxes which are the gross revenues minus refunds. Net revenue, therefore, reflects the “spendable” portion of the state’s tax revenue.

A. State Tax Revenues

Tax revenues are collected and reported on a fiscal year basis, and money is appropriated on a fiscal year basis. The state of Iowa’s fiscal year runs from July 1 to June 30.

The annual revenues collected from the various taxes imposed by the state of Iowa vary greatly from tax to tax depending on the tax base and the effective rate. In addition,

³²⁸ Iowa Code §453B.12(2)-(4). A class “D” felony is punishable by confinement for no more than five years and a fine of at least \$750 but not more than \$7,500.

³²⁹ Iowa Code §453B.15.

³³⁰ Iowa Code §453B.10.

³³¹ Iowa Code §165.18.

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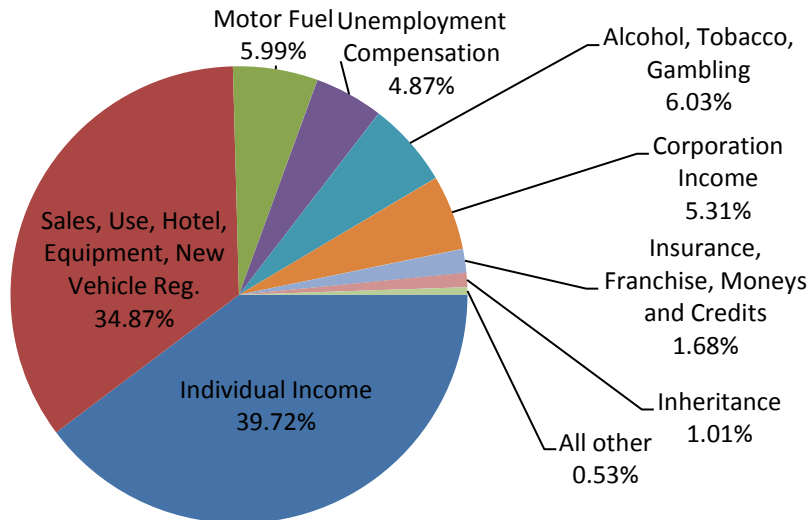
the amount of revenues from each tax can fluctuate greatly from year to year based on economic conditions, even if the rate and the tax base are unchanged.

Tax Type	FY 2015 Net Revenues
Individual Income	\$3,463,200,000
Sales, Use, Hotel, Equipment, New Vehicle Registration	\$3,040,632,000
Motor Fuel	\$522,100,000
Unemployment Compensation	\$424,685,000
Gambling	\$280,200,000
Corporate Income	\$463,200,000
Cigarette and Tobacco	\$222,600,000
Insurance	\$109,600,000
Inheritance	\$87,900,000
Franchise	\$36,400,000
Moneys and Credits	\$800,000
Environmental Protection Charge	\$21,500,000
Alcohol	\$22,600,000
Real Estate Transfer	\$19,400,000
Automobile Rental	\$4,500,000
Brucellosis and Tuberculosis Eradication	\$500,000
Drug Stamp	\$200,000



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Proportional Tax Revenue (FY 2015)



B. Local Tax Revenues

The following graph represents the amount of revenues from certain locally imposed taxes collected and administered by the state. The graph reports total, statewide revenue figures for these taxes and groups them in three primary categories: local option sales taxes, local income surtaxes, and local option hotel/motel taxes.

FY 2015 Revenues from Locally Imposed Taxes Administered by the State

■ Local Sales ■ Local Income Surtax ■ Local Hotel

\$324,100,000

\$100,700,000

\$52,700,000